

CORPORATE GOVERNANCE REPORT 2014

Rules and regulations and Articles of Association

Hufvudstaden is a Swedish publically listed company with its registered office in Stockholm. The Group is governed by the Articles of Association, the Swedish Companies Act, the rules of Nasdaq Stockholm for issuers, the Swedish Corporate Governance Code (the Code) and other applicable laws and rules. The Code aims to create good prerequisites for active, responsible ownership and is intended to be part of the self-governance process in Swedish industry, see www.bolagsstyrning.se. It is based on the principle of comply or explain, which means that companies can deviate from one or more rules in the Code if there is justification and an explanation and if the solution chosen can be presented.

Hufvudstaden complies with the Code with a deviation with regard to Election Committee stipulations. The deviation from the Code is explained in more detail below.

Shares and shareholders

Hufvudstaden's share capital at the year-end amounted to SEK 1,056,359,665, divided into 211,271,933 shares, giving a par value of SEK 5 per share. Of the shares, 202,996,869 are series A shares, carrying one vote per share, and 8,275,064 are series C shares, carrying 100 votes per share. All shares carry an equal right to a share in the Company's assets and profit. The largest shareholder is L E Lundbergföretagen AB, with a total of 45.3 per cent of outstanding shares and 88.1 per cent of the votes. Apart from L E Lundbergföretagen AB, there is no shareholder in the Company that holds, directly or indirectly, shares where the number of voting rights represents one-tenth or more of the total number of votes for all shares in the Company.

According to a conversion provision in the Articles of Association, the holders of series C shares are entitled to request that their series C shares be converted into series A shares. There are no limits in the Articles of Association regarding transferability of shares or voting rights at a general meeting of the shareholders. There are no known agreements that would be affected by a public purchase offer. There have been no infringements of applicable stock market rules. There is no pension fund or any other undertaking to the personnel with regard to shareholdings.

Buy-back of Company shares

Since the Annual Meeting in 2003, the Board of Directors has had the mandate of the General Meeting to buy back series A shares up to a maximum of 10 per cent of all shares in the Company. The mandate was renewed at the 2014 Annual Meeting. The aim is to give the Board the opportunity to adjust the capital structure in order to create increased value for the shareholders and/or to allow the Company's own shares to be used as liquidity in conjunction with or to finance the acquisition of a company or property. As at December 31, 2014, Hufvudstaden held 5,006,000 series A shares, equivalent to 2.4 per cent of the total number of shares. The whole block was acquired in 2003 at an average price of SEK 27.30 per share. No shares were bought back during the year or after the end of the reporting period (up to and including February 12, 2015).

Annual Meeting

A shareholder's right to decide in matters related to Hufvudstaden is exercised at a general meeting. Shareholders who are registered in the shareholders' register on the record date and who have notified their intention to attend the meeting within the specified time, are entitled to attend and vote at the Annual Meeting, either in person or by proxy. Shareholders who have their shares registered with nominees must, in order to exercise their right to vote at the Annual Meeting, have their shares re-registered temporarily in their own name as stipulated in the summons to the meeting. Decisions at the meeting are normally reached through a simple majority. In certain matters, however, the Swedish Companies Act stipulates that a proposal must be approved by a higher proportion of the votes represented and cast at the meeting.

Individual shareholders who wish to have a matter taken up at the meeting can make a request to the Hufvudstaden Board of Directors at a specific address, which is published on the Company's website, well in advance of the issuing of a summons to the meeting.

The Annual Meeting must be held in Stockholm within six months of the end of the financial year. The Annual Meeting makes decisions in a range of matters, including adoption of the Income Statements and Balance Sheets; dividend; discharge of the members of the Board of Directors and the President from liability; election of members of the Board of Directors, the Chairman of the Board and auditors, as well as remuneration to the Board of Directors and auditors; principles for remuneration to executives and other important matters. Notice of a general meeting shall be issued in the form of announcements in *Post-och Inrikes Tidningar* and on the Company's website. Notification that the summons has been sent out is published in *Dagens Nyheter*.

The 2014 Annual Meeting was held on March 20, 2014. A total of 385 shareholders, representing 127,423,647 series A shares and 8,261,295 series C shares, were present and they represented 953,553,147 votes, equivalent to 93 per cent of the total number of outstanding votes. Present at the meeting were the Board of Directors, the members of the Executive Management and the auditor. Fredrik Lundberg was elected to chair the meeting. It was decided at the Annual Meeting to adopt the presented Income Statement and the Balance Sheet as well as the Consolidated Income Statement and the Consolidated Balance Sheet and to allocate the unappropriated earnings in such a way that SEK 2.75 per share was paid to the shareholders as a dividend. At the meeting, discharge from liability was granted to the members of the Board of Directors and the President and a decision was reached on remuneration to the members of the Board of Directors and the auditors. In addition, all members of the Board of Directors and the auditors were re-elected for the period up to the end of the next Annual Meeting. Finally, a decision was reached at the meeting on guidelines for remuneration to executives and authorization for the Board of Directors to decide on the acquisition and transfer of the Company's own series A shares.

The 2015 Annual Meeting will be held in Stockholm on March 26, 2015.

Nomination and election of the Board of Directors and auditors

According to the Articles of Association, the Board of Directors shall comprise, in addition to the members appointed according to law by a party other than the general meeting, a minimum of five and a maximum of ten members. Members are elected at a general meeting of the shareholders for the period up to the end of the first Annual Meeting to be held after the year in which the members of the Board of Directors were appointed. In the light of the concentrated ownership structure, Hufvudstaden does not have a formally appointed Election Committee. The duty of an Election Committee to prepare the decisions to be reached at the Meeting in matters relating to elections and fees is handled by Hufvudstaden's main shareholder, LE Lundbergföretagen AB. The main shareholder proposes a person to chair the meeting, a Board of Directors, a Chairman and fees for the Board of Directors as well as an auditor and a fee for the auditor. Hufvudstaden must be notified of the proposal from the main shareholder well in advance to ensure that the proposal can be presented in the summons to the Annual Meeting and at the same time be presented on Hufvudstaden's website. Other shareholders have the opportunity to present nomination proposals at the address stated on the website. Proposals are made public no later than in conjunction with the summons to the Annual Meeting.

As a basis for its proposal prior to the 2015 Annual Meeting, the main shareholder has assessed whether the composition of the present Board of Directors is appropriate, among other things using applicable parts of the annual evaluation of the work of the Board of Directors as a guide. The Election Committee procedure applied at Hufvudstaden is a deviation from the Code.

Composition of the Board of Directors

Hufvudstaden's Board of Directors comprises nine members, elected at the Annual Meeting for a period of one year. The composition of Hufvudstaden's Board of Directors is arranged in line with the work of the Company. All members of the Board have been assessed based on skills, experience and background. The only member of the Executive Management on the Board is the President and he is the only one who can be regarded as being dependent on the Company. Fredrik Lundberg has been Chairman of the Board since 1998. Four of the members are in a position of dependence on the largest shareholder LE Lundbergföretagen AB (Fredrik Lundberg, Claes Boustedt, Louise Lindh and Sten Peterson). For further information about individual Board members, see pages 88 – 89. An external lawyer is engaged to act as secretary to the Board.

Responsibility of the Board of Directors

According to the Companies Act, the Board of Directors has overall responsibility for the Group's organization and management and for ensuring that control of the accounting records, management of funds and financial circumstances in general are satisfactory. The Board of Directors reaches decisions in matters regarding the Group's overall aims, strategic orientation and policies as well as more important issues regarding financing, acquisitions, divestments and investments. Other duties that are incumbent on the Board of Directors include the following:

- Continuous follow-up and assessment of the Company's financial position and business development.
- Continuous evaluation of the Company's operative management and the work of the President.
- Ensuring that there is satisfactory control of the Company's compliance with laws and other regulations and the continuous evaluation of the Company's internal control and risk management systems.
- Adopting the Company's ethical guidelines.

The work of the Board of Directors follows the rules of procedure adopted by the Board of Directors, which provide the framework for decisions regarding investments, financing, financial statements and other matters of a strategic nature. The rules of procedure also govern the undertakings of the Board of Directors and the President and the allocation of duties between the Board and the President. The relevance and validity of the rules of procedure are reviewed each year.

The Chairman of the Board leads the work of the Board of Directors and has continuous contact with the President to follow the Group's operations and development on an ongoing basis. The Chairman of the Board consults with the President on strategic matters, represents the Company in ownership matters and passes on the views of the shareholders to the Board.

The Chairman of the Board ensures that the work of the Board is evaluated once a year and that new Board members receive appropriate training. The Board also evaluates the work of the President, although without the person in question being present, and approves more material assignments carried out by the President outside the Company.

Work of the Board of Directors

During the 2014 financial year, the Board of Directors held seven meetings, of which one was a statutory meeting. Economic and financial reports and operational reports from the Business Areas are presented at each Board meeting. In addition, key matters of a principle nature or of major financial significance are taken up at each ordinary meeting. During the year, the work of the Board of Directors has been directed specifically at strategy discussions, issues pertaining to the economic climate and financing, property valuation and investments. Other matters dealt with during the year were upgrading of the Femman Shopping Precinct in Nordstan, development and refurbishment of the Härbärg block in Gothenburg and a review of the Company's finance policy. Company officials attend the Board meetings as presenters.

The Company's auditor attended the Board meeting in February when the Annual Report for 2013 was approved and the Board meeting in August in conjunction with the examination of the Company's six-monthly report.

Board committees

The Board has examined the matter of establishment of an Audit Committee but has chosen not to appoint such a committee and will instead handle matters that rest with such a committee as part of the regular work of the Board of Directors. The full expertise of the Board can be utilized and the meetings can be made more efficient. This means that the whole of the Board of Directors perform the duties that rest with an Audit Committee.

The Board of Directors has examined the question of setting up a Remuneration Committee but has opted not to set up such a committee and will instead handle the matter as part of the regular work of the Board of Directors. The full expertise of the Board can be utilized and the meetings can be made more efficient. This means that the whole of the Board of Directors, apart from the President, perform the duties that rest with a Remuneration Committee, including following up and evaluating programmes governing variable remuneration to executives, both current programmes and programmes that were concluded during the year. The Board of Directors also follows and evaluates the application of the guidelines governing remuneration to executives, as decided at the Annual Meeting, and governing Company remuneration structures and remuneration levels for executives.

Executive Management

The President heads operations in accordance with the adopted rules of procedure for the Board of Directors and the President, which include the instructions for the President issued by the Board of Directors. The President is responsible for ensuring that the Board of Directors receives information and a basis for making decisions that is sufficiently factual, complete and relevant for the Board of Directors to make well-informed judgements.

In addition to the President, the Executive Management comprises the three business area heads, as well as the Head of Accounting/Finance, the Head of Property Development and the Head of Human Resources. On October 1, 2014, one of the business area heads was appointed Vice President. The Executive Management meets approximately once a month to discuss current issues. For information about individual members, see pages 90 – 91.

Audit

According to the Articles of Association, the Company must have one or two auditors and a corresponding number of deputies. Alternatively, one or two registered auditing companies can be appointed. At the 2014 Annual Meeting, KPMG AB was re-elected as the auditing company for a period of one year. George Pettersson is lead auditor. George Pettersson's other major assignments include Holmen AB, Nobia AB, Sandvik AB and Skanska AB.

The Board meets the Company's auditor twice a year, once in the absence of the President. On these occasions, the auditor presents a report and there is a discussion about the audit orientation and observations. Internal routines and control systems are examined continuously during the year. A final examination of the annual accounts and the Annual Report takes place in January – February. The six-monthly report is examined on a general basis. The fee to the auditors, including the fee for advisory services, is reported in Note 9.

Remuneration

Board of Directors

Remuneration to the Board of Directors is decided at the Annual Meeting. At the Annual Meeting in 2014 it was decided that remuneration for Board work for 2014, totalling SEK 1,800,000, be divided among the members with the exception of the President, Ivo Stopner, who does not receive any remuneration for his work on the Board. The Chairman received SEK 400,000 and the other seven non-employed members received SEK 200,000 each.

Executive Management

Guidelines for salaries, bonuses and other remuneration to the Company's executives are decided at the Annual Meeting. It was decided at the meeting that the same guidelines decided at the 2013 Annual Meeting, with the exception of a direct pension for the President, should be applied for 2014, i.e. that the Company's remuneration shall comprise salaries in line with the market as well as a limited, profit-related bonus scheme as described below. The Company has no incentive schemes related to share price. These guidelines have been followed since the 2014 Annual Meeting. However, the Board of Directors has made a permitted deviation from the guidelines with regard to the Vice President entering an agreement regarding a defined contribution pension for the part of the salary not covered by the ITP plan. The agreement is equivalent to what has been agreed for the President. With the exception of an addendum regarding the possibility of a defined contribution pension to the Vice President, the guidelines that will be presented at the 2015 Annual Meeting are unchanged. The report by the Board of Directors covering the evaluation of variable remuneration programmes for the Executive Management, the application of guidelines for remuneration to executives and current Company remuneration structures and remuneration levels for executives will be published on the Company's website no later than two weeks prior to the 2015 Annual Meeting. The auditor's statement on whether guidelines for remuneration to executives, which were adopted at the Annual Meeting in 2014, have been followed will be available on the Company's website no later than three weeks prior to the Annual Meeting and will be attached to the documents distributed at the Annual Meeting. The statement is also available from the Company on request.

Remuneration to the President is proposed by the Chairman of the Board and is confirmed by the Board of Directors. The President does not take part in this decision. The President decides on remuneration to other executives following consultation with the Chairman of the Board.

For further information regarding salaries and remuneration as well as guidelines for remuneration to executives, as adopted at the 2014 Annual Meeting, see Note 8.

Bonus

Other permanent employees in the Group were included in a bonus scheme during the year. The bonus payment criteria are 'operating results' and 'customer satisfaction'. In the case of managers with HR responsibility, there is also a personal assessment with individual objectives.

In the case of both bonus schemes, a decision is made one year at a time and the bonus is subject to a ceiling. A bonus is only payable if the Company reports a positive result with no consideration given to unrealized changes in value. In 2014, the bonus cost for all employees was SEK 1.7 million (3.1) or an average of SEK 9,000 per employee. For the Executive

Management, including the President, the average was SEK 120,000 per person.

Internal control and risk management

The Board of Directors has overall responsibility for ensuring that Hufvudstaden has a satisfactory internal control system. The President is responsible for ensuring that such a system is in place and covers any material risk of error in the financial statements. Hufvudstaden's internal control systems cover the control environment, risk assessment, control measures, information, communication and follow-up.

Control environment

The control environment is the basis for internal control of financial reporting. Hufvudstaden's internal control structure is based, among other things, on a clear allocation of responsibility and duties between the Board of Directors and the President and within the Company's operations. The Executive Management and the Board of Directors continuously document and evaluate policies and guidelines, such as the Company's valuation principles, information policy and accounting handbook. To ensure continuous operational follow-up, there are routines in place for financial reporting and analysis. The routines include monthly and quarterly reports, budget follow-ups and forecasts. These tasks are handled by the accounting and controller function on the Business Area and Group level.

Risk assessment

Based on ongoing discussions and meetings in the organization, the Hufvudstaden Executive Management identify, analyze and decide on the Company's material risk areas, whereupon the Board of Directors confirms these areas. The Executive Management is responsible for handling the risk of error in the financial statements. The Board of Directors examines the outcome of the Company's risk assessment and risk management process to ensure it covers all material areas. Hufvudstaden's greatest risks are linked to property valuation, financial transactions, property projects and handling of tax matters.

Control measures

Based on risk assessments, Hufvudstaden has adopted a number of control measures. These are both of a preventative nature, i.e. measures aimed at avoiding losses or errors in the reporting, and of an identification nature. The controls should also ensure that errors are rectified. Examples of areas that have a material impact on the Company's result, and which have carefully formulated control measures, are property and derivative valuation, maintenance, redevelopment, interest payments and leasing. Controls are carried out, among other things, using deviation analyses and quarterly meetings between the business area, group management and controller function.

Information and communication

In-house information and external communication are governed on a general level by, among other things, an information policy. Internal communication to and from the Board and Executive Management takes place, among other things, by the management holding regular information meetings, both for the whole Company and for individual units. Another important communication channel is Hufvudstaden's intranet. Through the intranet, all employees have access to up-to-date information. Internal policies, guidelines, instructions and equivalent documents that control and support operations are published on the intranet. Feedback on internal control work takes place at quarterly meetings, management team meetings and Board meetings.

Follow-up

The Hufvudstaden Executive Management evaluates on an ongoing basis internal control of financial reporting, particularly through its own analyses, questioning and familiarization with the work of the controller function. To follow up identified risks and ensure that the internal control work takes place optimally, the controller function works continuously on this follow-up process. Apart from quarterly reports with financial outcomes, including the Executive Management's comments on operations, the Board receives the Executive Management's comments on how internal control is working and whether identified risks ought to be changed. The Company's auditor attends Board meetings on two occasions each year and reports his observations regarding the Company's internal routines and control systems. The members of the Board then have the opportunity to ask questions. Each year, an examination is made of material risk areas, whereupon the Board adopts a position on risks in the financial reporting system and evaluates the internal controls.

Internal audit statement

The Hufvudstaden Executive Management has systematically examined and structured the internal documentation of the in-house control system. Nothing has emerged to indicate that the control system is not functioning in the manner intended. The Board of Directors has therefore decided not to establish an internal audit function. This decision will be reviewed annually.