

Corporate governance report

Following is information on corporate governance in accordance with the Swedish Code of Corporate Governance ("the Code") for the 2010 financial year. Vattenfall's Articles of Association, previous corporate governance reports, material from the most recent general meetings and other documents are available on Vattenfall's website, www.vattenfall.com, under "Corporate Governance".

2010 year's corporate governance report has been read by the company's auditors, without comment (see Auditor's report on the corporate governance statement in the Audit report, page 135).

Important internal and external regulatory systems

The Parent Company of the Vattenfall Group, Vattenfall AB, is a Swedish public limited liability company with registered office in Stockholm. The Swedish Companies Act thus applies for Vattenfall AB, which entails that the company shall have a board of directors that is elected by the Annual General Meeting (AGM). The Board, in turn, appoints the President and CEO, who is responsible for the day-to-day

administration of the company in accordance with the Board's guidelines and instructions. The AGM also decides on Vattenfall AB's Articles of Association, which specifies the object of the company's business, among other things.

Corporate governance in the Group is based on:

- Swedish and foreign legal rules;
- The Swedish state's ownership policy and other owner directives;
- The Swedish Code of Corporate Governance ("the Code");
- The Articles of Association;
- The Board's Rules of Procedure, including the CEO instruction and instructions on reporting to the Board of Directors;
- Internal documents – particularly Vattenfall Management System (VMS); and
- The Swedish Annual Accounts Act.

Vattenfall also adheres to the stipulations that apply for companies registered on Nasdaq OMX Stockholm, in Swe-

den, as well as in the other marketplaces in which Vattenfall has securities registered.

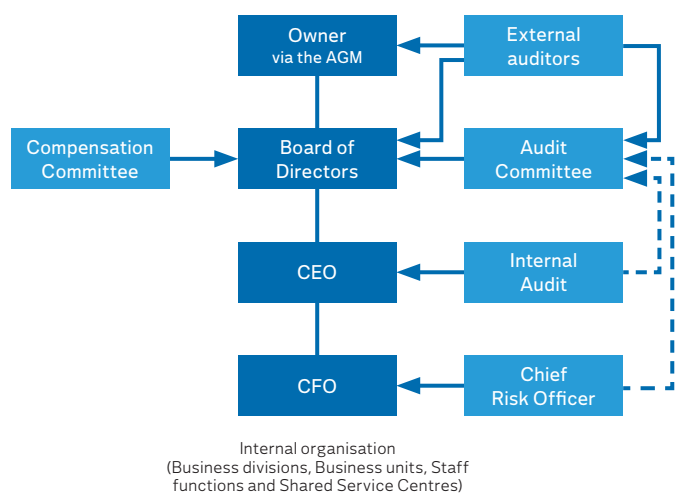
The departures that Vattenfall makes from the Code are mainly due to the company's ownership structure: Vattenfall is 100%-owned by the Swedish state, while the Code is written primarily for listed companies with broad ownership. Moreover, due to these ownership conditions, certain stipulations are not even applicable for Vattenfall.

Departures from the Code are specified in the table below.

Annual General Meeting and owner

According to Vattenfall's Articles of Association, the Annual General Meeting (AGM) shall be held within six months after the end of each financial year. The AGM elects, on the recommendations of the owner, the Board of Directors and auditors, adopts the income statement and balance sheet, and deals with other matters of business that are incumbent upon the Meeting pursuant to the Swedish Companies Act or the Company's Articles of Association.

Governance and reporting structure



Departures from the Code

Vattenfall's corporate governance for the 2010 financial year departs from the requirements stipulated in the Swedish Code of Corporate Governance on the following points.

Code requirement	Description	Chosen solution and justification
1.3 The Board's quorums at Extraordinary General Meetings	As many board members shall be present at general meetings that the Board has a quorum.	A majority of the board members were present, but not as many so as to constitute a quorum as stipulated in the Articles of Association.
1.4 Chairman to preside over the Annual General Meeting	The nomination committee shall propose a person to serve as AGM chairman.	Due to its ownership structure, Vattenfall has no nomination committee. Election of an AGM chairman is instead done at the AGM in accordance with the stipulations of the Swedish Companies Act. This is also in line with the Swedish state's ownership policy.
2. Nomination committee	The company shall have a nomination committee.	Due to its ownership structure, Vattenfall has no nomination committee. The nomination process is instead conducted in accordance with the Swedish state's ownership policy. Nor are the references to the nominating committee in points 1.3, 4.6, 8.1 and 10.2 thereby applicable either. However, information on the nomination of board members for new election or re-election is posted on the website in accordance with point 2.6.

Vattenfall's Annual General Meeting was held on 29 April 2010, in Stockholm. The AGM adopted the annual report and consolidated financial statements for 2009 submitted by the Board of Directors and CEO, resolved to distribute the company's profit and discharged the members of the Board and the CEO from liability.

All re-elected and newly elected directors were in attendance at the AGM, except for Eli Arnstad, who was not able to attend. As in previous years, the meeting was open to the general public, and an open Q&A session was arranged, in accordance with the Swedish state's ownership policy. Members of Parliament were given the right to ask questions, as stipulated in Vattenfall's Articles of Association. The meeting was aired live via webcast. A recorded version of the AGM can be viewed on Vattenfall's website, along with the minutes and other material from the AGM.

Due to Vattenfall's ownership structure, no information is provided on the company's website on shareholders' opportunity to submit items of business for the AGM. The Code's stipulations about this are not applicable for Vattenfall.

Extraordinary General Meeting

On 23 August 2010 Vattenfall held an Extraordinary General Meeting, at which a resolution was passed to amend the Articles of Association. The reason for this was that on 3 June 2010 Sweden's parliament (the Riksdag), pursuant to a government bill (2009/10:179), decided in favour of a clarification of the assignment for Vattenfall AB. According to the Riksdag's decision, the company's assignment shall be to generate a market rate of return by operating a commercial energy business that enables the company to be among the leaders in developing environmental sustainable energy production. The operational description in the Articles of Association was amended to reflect this changed assignment. The new Articles of Association are posted on Vattenfall's website, www.vattenfall.com, under "Corporate governance".

The Board's composition Appointment of the Board

For enterprises that are wholly owned by the

Composition of the Board and meeting attendance

Name	Function	Nationality	Independence in relation to the company and company management (according to the Code)	Committee assignments	Total fees/ (SEK 000s) per year 2010	Attendance at board meetings	Attendance at committee meetings
Lars Westerberg	Chairman of the Board	Swedish	Yes	Remuneration Committee	580	14/14	7/7
Carl-Gustaf Angelin	Employee representative	Swedish	–		13	13/14	
Eli Arnstad	Director	Norwegian	Yes		280	12/14	
Johnny Bernhardsson	Employee representative	Swedish	–		13	14/14	
Christer Bådholm	Director	Swedish	Yes	Audit Committee (chair)	350	14/14	5/5
Lars Carlsson	Employee representative, deputy	Swedish	–		13	13/14	
Ronny Ekwall	Employee representative, from 12 April 2010	Swedish	–		–	10/10	
Lone Fønss Schrøder	Director	Danish	Yes	Audit Committee	350	12/14	4/5
Lars-Göran Johansson	Employee representative, deputy	Swedish	–		13	14/14	
Patrik Jönsson	Director, from 29 April 2010	Swedish	Yes	Remuneration Committee, Audit Committee, both from 29 April 2010	–	10/10	CC: 4/4 AC: 3/3
Per-Ove Lööv	Employee representative, deputy, from 12 April 2010	Swedish	–	Audit Committee, from 12 April 2010	–	10/10	4/4
Björn Savén	Director	Swedish	Yes		280	14/14	
Cecilia Vieweg	Director	Swedish	Yes	Remuneration Committee (chair) from 29 April 2010	280	13/14	7/7
Viktoria Aastrup	Director, through 29 April 2010	Swedish	Yes	Remuneration Committee (chair), Audit Committee; both through 29 April 2010	117	4/4	CC: 3/3 AC: 2/2

Note: The 2010 AGM resolved that no fees shall be payable to employee representatives or to the board member who is employed in the government offices.

Swedish state and that are not listed in a marketplace, uniform and joint principles for a structured nomination process are applied, which take the place of the Code's rules on drafting work for decisions on the nomination of board members and auditors. The nomination process is co-ordinated by the State Enterprises Division of the Ministry of Finance. A work group analyses competency needs based on the company's operations, situation and future challenges, as well as the composition of the respective boards. Thereafter, any recruitment needs are determined and recruitment work is initiated. Board members are chosen from a broad recruitment base in the aim of benefiting from the expertise of women and men as well as of individuals with varying backgrounds and experience. Once this process has been completed, any nominations are to be publicly announced in accordance with the Code's guidelines; however, no report is made on the directors' independence with respect to the state as a major shareholder. Vattenfall provides orientation training for new directors who are elected by the AGM.

Additional stipulations on the nomination of board members are set forth in the Swedish state's ownership policy (N2010.24).

Board members

Vattenfall's Articles of Association stipulate that the Board shall have a minimum of five and a maximum of ten members, for the part of the Board that is elected by the AGM. In 2010 Vattenfall's board included seven AGM-elected directors. By law, the unions are entitled to appoint three board members plus three deputies. Through 12 April 2010 the unions had two members and two deputies on the Board, and for the time thereafter three members and three deputies. No members of the Executive Group Management (EGM) are members of the board. Thus in accordance with the Swedish state's ownership policy, nor is the CEO a member of the Board. Of the board members, three are women and two are foreign citizens. The average age of board members in 2010 was 56.

The work of the Board

Duties and delegation of work on the Board

The matters reserved for the Board are prescribed primarily by the Swedish Companies Act and the Board's Rules of Procedure. The main duties of the Board, apart from appointing the CEO and executive vice presidents, are:

- to set Vattenfall's strategy;
- to ensure that Vattenfall has effective management and to monitor and control the organisation and administration of the Executive Group Management;

- to ensure that Vattenfall has good internal control, including risk management, and to stay continuously informed about and evaluate how the systems of internal control work;
- to continuously assess Vattenfall's financial situation;
- to ensure that the organisation of Vattenfall's bookkeeping and treasury management include means of maintaining satisfactory control; and
- to continuously control the extent to which the CEO is fulfilling his responsibility for the day-to-day administration.

In addition, the Board shall approve major investments, acquisitions and divestments, and set central policies and instructions.

Each year the Board establishes its Rules of Procedure. Apart from mandatory items stipulated by the Swedish Companies Act, the Rules of Procedure regulate such matters as the Chairman's duties, information provided to the Board, the form of board meetings, the establishment of board committees, and evaluation of the work of the Board and the CEO.

The Chairman leads the work of the Board and is responsible for ensuring that other board members receive adequate information. The Chairman participates when necessary in important external contacts.

The Board has established within itself an audit committee and a Remuneration Committee, along with rules of procedure for the committees. In addition, the Board can, where necessary, establish other committees to look into matters in more defined areas. In other respects, the Board shall not delegate any special areas of responsibility or duties among its members.

Assuring the quality of financial reporting

In the section on internal control (page 71), the Board has reported on the company's internal control structure for the financial reporting routines. The Audit Committee's work is a part of this control exercised by the Board. At all Audit Committee meetings in 2010, external and internal auditors reported their observations concerning the full-year and half-year book closing, among other things. In conjunction with planning work for the annual audit, discussions are held between the external auditors and the internal audit unit concerning Vattenfall's risk situation.

The Board's risk management process

Vattenfall's Chief Risk Officer (CRO) is responsible for organisation of risk management within the Group. The CRO is responsible for this organisation at Group level and is responsible for informing the Audit Committee about his/her observations regarding the Group's risks.

The Board sets the overall risk mandates for the Group in the areas of energy and commodity trading, as well as for financial, insurance and credit risks. At each meeting, the Board receives information about the Group's financial position, including a report on outstanding guarantees and risks. The Board also holds an annual risk management seminar at which a more in-depth review is made of the Group's financial and operational risks.

For a more detailed description of Vattenfall's risks and risk management, see pages 77–83.

Description of the Board's work

The Board's Rules of Procedure stipulate that five to eight regular meetings are to be held each year. In addition to the regular meetings, the Board is summoned to further meetings if the need arises. The Rules of Procedure stipulate, among other things, that the following items are to be included on the agenda once a year:

- The Group's strategic plan;
- The Group's total risk exposure;
- Safety and environmental issues in the nuclear power operations;
- Review of strategic personnel issues within the Group, including competence succession; and
- Research and development activities within the Group.

In addition, at every regular meeting a report is presented on important business events since the previous meeting as well as on the financing situation. Investments are followed up and analysed by the Board three years after the Board's decision to invest.

The Board also holds a number of board seminars each year. At these seminars the Board receives more detailed information about and discusses Vattenfall's long-term development, strategy, competitive scenario and risk management.

The Board met 14 times in 2010, including the statutory meeting. A quorum existed at all meetings. According to the Rules of Procedure, at least one meeting every year is to be held at another location than the head offices. In 2010 a meeting was held in Stora Sjöfallet and Gällivare, Sweden. This meeting was combined with a visit to Vattenfall's hydro power facilities in the area.

In addition to the items of business prescribed for a board decision by the Rules of Procedure, in 2010 the Board dealt with and decided on the following matters:

- New strategic direction (see below);
- Appointment of a new CEO; and
- The Group's nuclear power operations.

Board decision on new strategic direction

On 24 August and 20 September 2010, the Board decided on a new strategic direction, organisational structure and business model for the Vattenfall Group. These decisions were prompted by, among other things, the amendment to the Articles of Association that was adopted by the Extraordinary General Meeting on 23 August.

The new strategic direction is intended to increase focus on profitability and value creation as well as focus on the core markets (Germany, Sweden and the Netherlands), on three main products (electricity, heat and gas) lower CO₂ exposure, and growth in low CO₂-emitting energy production and in gas. Vattenfall thereby aims to be a leader in developing environmental sustainable energy production. The decision entails that Vattenfall will continue to be an integrated European company with a diversified energy portfolio. The geographic focus shall be on Sweden, Germany and the Netherlands. Vattenfall also decided to introduce a business-led organisational structure.

Evaluation of the Board's and CEO's work

The Board evaluates its own work and the CEO's work once a year through a systematic and structured process in the aim of developing the Board's work forms and effectiveness. This evaluation is headed by the Chairman and is reported to the Board. The most recent evaluation was presented at the board meeting on 14–15 December 2010.

Committees

Audit Committee

The Audit Committee is a board committee that is tasked with the following duties, among others:

- Assisting the Board on matters pertaining to financial risk and reporting, as well as external and internal audit;
- Conducting preparatory work for the Board in quality assuring Vattenfall AB's financial reporting;
- Monitoring the effectiveness of internal control, internal audit and risk management;
- Assisting the owner in the selection of auditors and setting of fees for the audit activities;
- Evaluating the work of the external auditors;
- Setting guidelines for other services than auditing that Vattenfall AB and the Group may purchase from the company's auditors; and
- Approving the internal audit plan.

The Audit Committee has special responsibility for the work on application of the Code and for preparing required

reports. The CFO, the Head of Internal Audit and the Chief Risk Officer make presentations at Audit Committee meetings. In addition, the company's auditors attend all meetings and report their observations regarding the audit.

The Board of Directors has authorised the Audit Committee to – on behalf of the Board – approve the quarterly reports for the third quarter of 2010 and first quarter of 2011, i.e., the reports that are not formally reviewed by the auditors. However, the Board as a whole shall be convened for a review and approval of these reports if the Audit Committee is of the opinion that this should be done. In addition to this authorisation, the Audit Committee has the right to approve Internal Audit's budget and yearly plan as well as the guidelines for procuring services from the auditors. In other respects, the committee has no decision-making right.

The Board has adopted rules of procedures for the Audit Committee. The committee reports its work to the Board through the committee chair, who informs about the committee's decisions, and by submitting meeting notes to the Board.

Remuneration Committee

The Board has established a Remuneration Committee that is tasked with the following, main duties:

- Ensure implementation and compliance with the guidelines for terms of employment for senior executives that have been adopted by the Annual General Meeting;
- Conduct drafting work for the Board's proposed principles for compensation of the CEO and other senior executives ahead of the 2011 Annual General Meeting;
- Conduct drafting work for the Board's proposal for updated guidelines when a need arises;
- Conduct drafting work for ongoing matters concerning compensation and other terms of employment for the CEO, ahead of the Board's decisions, and to serve as a control body for the CEO's proposal for compensation and other terms of employment for senior executives (encompassed within the annual salary review);
- Where applicable, to conduct drafting work for any special reasons that may exist in an individual case to depart from the guidelines; and
- Review the Board's report on compensation of senior executives in the Annual Report and, ahead of the 2011 Annual General Meeting, to monitor and follow-up the auditors' review.

The Remuneration Committee has evaluated the application of the guidelines for compensation of senior executives in

2010 and conducted drafting work for the Board's reporting and proposals ahead of the Annual General Meeting.

The Head of Human Resources and employee responsible for salaries and benefits in Group Function Human Resources make presentations at the committee's meetings. The Board has adopted rules of procedure for the committee's work. The committee reports its work to the Board through the committee chair, who informs the Board about the committee's decisions, and by distribution of meeting notes to the members of the Board of Directors. The Board has not delegated decision-making right to the Remuneration Committee, and it is thus the entire Board's responsibility to decide on such matters as employment of the CEO, setting the level of compensation for the CEO and deciding on other terms of employment.

Compensation guidelines

Directors' fees

Directors' fees and fees for committee work are set by the AGM, based on the Swedish state's ownership policy. For information on directors' fees in 2010, see the table "Composition of the Board and meeting attendance" on page 65, and Note 50 to the consolidated accounts in the Annual Report.

Compensation of senior executives

The AGM has resolved (in 2009 and 2010) that the Swedish government's guidelines (20 April 2009) for terms of employment for senior executives of state-owned companies (government's guidelines) shall apply to Vattenfall AB. The government's guidelines pertain to companies in which the state, through its ownership, has a controlling interest, such as by owning more than 50% of the votes.

Such companies shall apply the guidelines in their subsidiaries. By subsidiary is meant in the government's guidelines such legal entities referred to in Ch. 1 § 11 of the Companies Act (2005:551).

One aspect of the government's guidelines is that variable salary shall not be paid to senior executives, and that contracts including provisions for variable salary shall be renegotiated. By senior executives is meant in the government's guidelines the CEO and other members of the company's management. This group corresponds to the persons referred to in Ch. 8 § 51 of the Companies Act. For example, it includes persons included on management teams or similar bodies and managers who are directly subordinate to the CEO.

At the AGM, the Board shall report on whether previously decided guidelines have been adhered to or not, and the reasons for any deviations from the guidelines. The Board

shall also report on any special reasons that may exist in a specific case for deviating from the guidelines.

In application of the government's guidelines, Vattenfall deviates from them with respect to how they have been applied in Vattenfall's subsidiaries. The Board is of the opinion that the following, special reasons exist for deviating from the government's guidelines.

Vattenfall's main reasons for deviating from the government's guidelines are the difficulties and costs associated with renegotiating existing contracts for executives who, according to the government's guidelines, should have been defined as senior. In the view of Vattenfall's board, renegotiation of a large number of contracts with national variations would be very time-consuming, entail a significant risk of losing key competence, and involve unreasonable costs.

For commercial and legal reasons, the Vattenfall Group has more than 400 subsidiaries. A very large number of executives would thereby be considered to be senior in application of the government's guidelines also in subsidiaries. Moreover, like other international groups, Vattenfall governs its operations based on a commercial focus (via the business areas) and not primarily according to the legal company structure.

To determine in a systematic way which executives can be considered senior in the Vattenfall Group, the established international ranking model IPE (International Position Evaluation) has been used. In this context, size in the form of sales, number of employees and number of levels in the value chain, as well as demands on innovation, knowledge, strategic/visionary role and international responsibility of the executive have played a decisive role. In addition to serving as a guide in defining senior executives, the international ranking model IPE has also been used as support for comparing managers' salaries in a systematic way and as documentation for the setting of salaries and management planning for senior executives. Aside from use of the IPE model, external experts have been consulted to analyse practice regarding the relation between fixed and variable salary in the countries in which the Vattenfall Group is active. Expertise in international labour law has been consulted to obtain a picture of the legal status, including opportunities to renegotiate existing contracts.

Vattenfall's conclusion of the analysis is that, in addition to the Executive Group Management, managers with positions from IPE 68 and above shall be considered to be senior within the Group. However, all senior executives (as defined in the government's guidelines) of all subsidiaries were included in Vattenfall's analysis.

Fifteen positions have thereby been identified for 2010. Of these, ten individuals are members of the Executive Group Management, and the others are executives employed by subsidiaries who have an IPE ranking of 68 or higher. Principles and computations for converting variable to fixed salary have been drawn up. In connection with the annual review of senior executives' salaries in 2010, individual reviews were performed.

In addition, Vattenfall's German subsidiaries have a number of employment contracts with senior executives active in those companies which deviate from the government's guidelines' stipulations on the maximum permissible notice period and severance pay. According to the government's guidelines, the notice period for a senior executive in the event the company serves notice shall not exceed six (6) months. The government's guidelines also allow, in cases where the company serves notice, payment of severance pay equivalent to a maximum of eighteen (18) months' salary. In the event the individual in question accepts new employment or receives income from business activities, the remuneration from the company serving notice shall be reduced by an amount corresponding to the new income during the time termination salary and severance pay are paid out. Vattenfall's German subsidiaries have a number of employment contracts with senior executives active in those companies, which have fixed contract periods and which therefore do not contain stipulations for a notice period or severance pay and thus do not include any stipulations on deduction of income from new employment from remuneration from the company serving notice in connection with termination. Practice in Germany for these contracts has entailed a contract period of sixty (60) months, i.e., five years; however, the trend is moving increasingly toward shorter contract periods – often for thirty-six (36) months, i.e., three years. The contracts cannot – except for under exceptional circumstances – be cancelled prematurely and could therefore entail, with respect to senior executives who have more than twenty-four (24) months remaining in their employment contracts, a cost for the companies that deviates from the guidelines in the event the companies should want to terminate the executives' employment before the end of the contract period. This situation has already arisen in three cases, where in accordance with German rules and contracts, the companies have been obligated to pay remuneration that deviates from the government's guidelines in connection with termination of the senior executives' assignments.

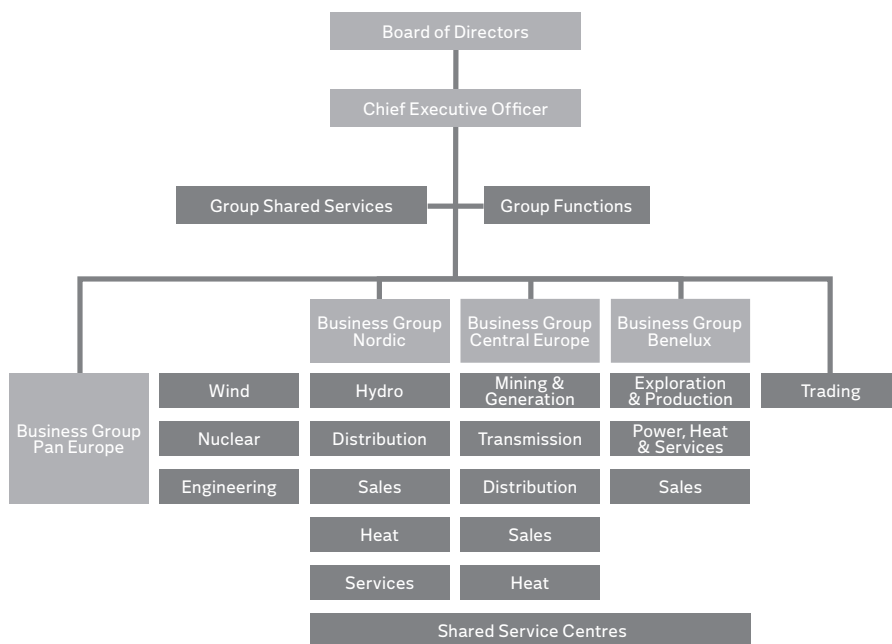
Further deviations from the government's guidelines pertain to two aspects of the conditions for pension benefits for

Building blocks of the management system

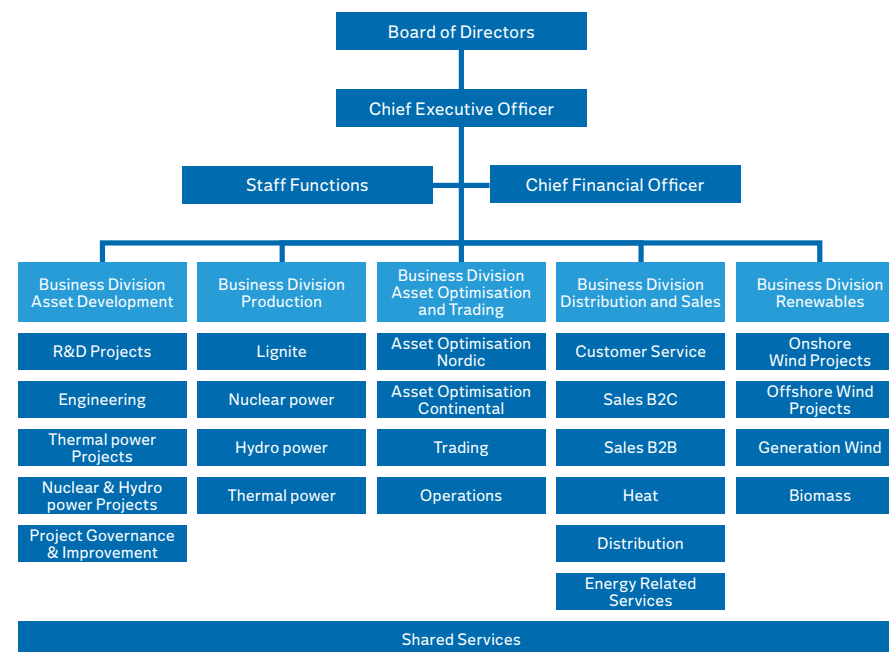


the senior executives active in Vattenfall's German subsidiaries. According to the government's guidelines, defined benefit pension solutions shall follow the applicable collective pension plan, which must be interpreted as the pension plan that follows from the applicable (Swedish) collective bargaining agreement. These conditions are, for obvious reasons, not fulfilled in relation to five senior executives with defined benefit pension solutions in accordance with German practice. Furthermore, it is prescribed in the government's guidelines that the retirement age shall not be below 62 years of age. Three senior executives of Vattenfall's German subsidiaries are entitled to early retirement from the age of 59. However, two of these executives will not reach the age of 59 during the term of employment. The third individual is relieved from his duties during the remaining part of the term of employment.

Vattenfall's organisational structure 2010



Vattenfall's organisational structure 2011



In addition, three senior executives of these companies are entitled to early retirement in case of permanent incapacity to work, without any connection to a certain age.

The reason for the deviations is that the contracts between the German Group companies and the senior executives active in those companies have been drawn up in accordance with German law and German practice, which entail that long fixed-term contracts are an important component in the security systems that make it possible for Vattenfall to attract and retain senior executives in Vattenfall's operations in Germany. In recent years Vattenfall has made an adjustment entailing that, as a rule, Vattenfall offers three-year assignments instead of five-year assignments as previously. In the future, Vattenfall will continue this adaptation in order to find solutions that ensure adherence to the government's guide-

lines while still giving Vattenfall the opportunity to attract and retain senior executives in Germany.

A description of the remuneration paid out to the former President and CEO in connection with his resignation is set out in Note 50 to the consolidated accounts.

For senior executives, as defined by Vattenfall, only fixed salaries exist. In addition, no share-based or share price-related incentive programmes exist for the Board of Directors or Executive Group Management. Taxable remuneration and benefits and pension costs for the Chairman of the Board, board members, the CEO and members of the Executive Group Management, and compliance with the guidelines set by the 2010 AGM for compensation of senior executives, are described in more detail in Note 50 to the consolidated accounts.

Auditors

The Swedish state's ownership policy states that responsibility for election of auditors of state-owned companies shall always rest with the owner by decision of the Annual General Meeting. Vattenfall's Articles of Association stipulate that a minimum of one and maximum of three auditors are to be appointed at the Annual General Meeting, along with a minimum of one and a maximum of three deputies, and that a chartered auditing firm can be appointed as auditor or deputy auditor. In accordance with the Act on Audits of State Enterprises, the Swedish National Audit Office can appoint one or more auditors to participate in the annual audit. When re-election of auditors is being considered, the auditors' work is always evaluated.

The 2008 Annual General Meeting appointed the audit-

ing firm Ernst & Young AB as auditor, with Authorised Public Accountant Hamish Mabon as auditor-in-charge. This appointment applies for a term until the 2012 AGM. Apart from his assignment for Vattenfall, Hamish Mabon is auditor for the following companies: Hexagon AB, Scania-Bilar Sverige AB, Softronic AB and Ambea AB.

The Swedish National Audit Office has appointed Authorised Public Accountant Per Redemo to serve until the 2012 AGM, with Authorised Public Accountant Göran Selander as deputy during the same time period. Per Redemo has held this position since 2004. Per Redemo is also the National Audit Office's auditor for SJ AB.

None of the auditors has assignments for companies that affect their independence as an auditor of Vattenfall.

The auditors reported on their audit of the year-end book-closing to the entire board at the board meeting on 11 March 2010, and also reported on their remarks at the board meeting on 14–15 December 2010. In connection with the report on 11 March 2010, the Board met the auditors without the presence of the CEO or other person from management. The auditors also provided more detailed reports at meetings of the Audit Committee. In addition, the auditors meet Vattenfall's CEO and CFO on numerous occasions during the year.

The Audit Committee has approved guidelines for how procurement of other services than auditing shall take place. These guidelines apply for all of the Group's external auditors. In cases where more extensive consulting activities are to be performed by the elected auditors, the assignment must first be discussed and approved by the Audit Committee or CFO. The Group's auditing costs are described in more detail in Note 53 to the consolidated accounts and Note 40 to the parent company accounts in the Annual Report. Consulting provided by Ernst & Young AB from 2008 to 2010 pertained primarily to taxation and accounting issues, as well as to studies regarding project routines.

Management and management system

CEO and Executive Group Management

The President of Vattenfall AB, who is also CEO of the Vattenfall Group, is responsible for the day-to-day administration in accordance with the Swedish Companies Act. The President has appointed decision-making bodies for the Group and makes decisions independently or with the support of these decision-making bodies.

Lars G. Josefsson was President and CEO through 11 April 2010. The Board decided on 11 March to appoint Øystein Løseth as President and CEO effective 12 April.

The Executive Group Management (EGM) focuses on the

Group's overall direction and decides – within the framework of the CEO's mandate from the Board of Directors – on matters of importance for the Group, such as certain acquisitions, investments and divestments (compare with the section "The work of the Board", on page 66). Information on the members of the Executive Group Management is provided on pages 74–75.

Governing business ethics

The Executive Group Management decided on 12 August 2010 that Vattenfall's core values shall be Safety, Performance and Co-operation.

Vattenfall's vision is to develop a sustainable, diversified European energy portfolio with long-term increased profits and significant growth opportunities. At the same time, Vattenfall will be among the leaders in developing environmentally sustainable energy production.

Vattenfall's Group-wide Code of Conduct and company philosophy stipulate that all employees shall adhere to and work in accordance with Vattenfall's core values, policies and instructions. The stipulations of the Code of Conduct are concretised in other parts of the management system. Work is currently in progress on drawing up a new Code of Conduct. In 2010 Vattenfall also completed the introduction of a Group-wide whistleblowing function with locally appointed external ombudsmen (advocates) to whom employees, consultants and contractors can turn to report suspected, serious improprieties that the "whistleblower" for some reason does not want to report internally via the normal reporting channels. Further information on guiding business ethics is provided in Vattenfall's Corporate Social Responsibility Report.

General information on the Vattenfall Management System (VMS)

In 2010 the Group was governed with a focus on value creation and long-term overarching goals and requirements for the Business Groups and business units. The Business Groups proposed short-term goals for each business unit, which were subsequently approved by the CEO and the Executive Group Management (EGM).

To ensure that Vattenfall develops in the intended direction and lives up to ethical and legal requirements, the CEO has established the Vattenfall Management System (VMS). Integrated with the VMS is an Environmental Management System. The VMS is available to all employees on the Group's intranet. The VMS consists of a number of building blocks (see illustration on page 68) and is documented in binding governing documents.

The Group's management processes for strategic planning, business planning and follow-up have been central governance tools for the Executive Group Management. The Group functions have been responsible for proposing, developing and following up binding governance documents. The Group's Quality function has had a co-ordinating role for the management system and has had a decision-making committee tasked with establishing adherence and improvements to the VMS. In addition, certain central documents have been approved the Vattenfall AB Board. All units within Vattenfall are obligated to comply with the management system's governing documents.

Special routines are in place to ensure that the VMS is also applied by subsidiaries. With respect to the German subsidiaries, since June 2008 a special agreement (Beherrschungsvertrag) has been in place between Vattenfall AB and the German holding company, Vattenfall Europe AG. Under this agreement, the board (Vorstand) of the holding company is subordinate to Vattenfall AB, and Vattenfall AB has the right to issue directives regarding governance.

Organisation and processes

The following applied in 2010 with respect to Vattenfall's organisation and processes. (For information about the new organisational structure for 2011, see the subheading that follows).

During the year, Vattenfall's organisational model was based on the value chain for electricity (generation, transmission, distribution and sales) and for heat (production, distribution and sales). Reporting and follow-up of the business activities were conducted with full transparency in accounting, control, profitability and value creation.

In terms of governance, Vattenfall's operations were broken down into three categories:

- Business activities handled by the Business Groups and their business units;
- Functions that supported their respective management teams; and
- Shared Service units, which provided and developed services that supported the business units and other users' efforts to optimise their business activities.

The organisation for 2010 is illustrated on page 69.

A number of important processes have been in place to facilitate governance within the Group. Each process is managed by a process owner, usually a member of the EGM, who is responsible for developing the process. In 2010 the following Group processes were in place: strategic and business

planning, reporting and follow-up, risk management, M&As, investments, communications, management development and asset management.

The strategic and business planning process culminates in yearly strategic and business plans. This process includes the analysis, evaluation and assessment of strategic issues along with EGM decisions on selection, formulation and priorities. Strategic planning includes the Group's long-term operations as well as its financial performance. Each year a strategic plan is drafted for decision by Vattenfall's board. Based on the directives of the strategic plan, the Business Groups and business units draw up one-year plan and a five-year plan containing a strategic direction. These plans are subject to the ultimate approval of the EGM. The Group's financial plan for the following calendar year is ultimately adopted by the Board.

New organisational structure

On 24 August and 20 September 2010 the Board decided on a new strategic direction, organisational structure and business model for the Vattenfall Group. As part of this, a new, business-led organisational structure is also being introduced for the Vattenfall Group. The new organisational structure took effect on 1 January 2011 and entails the primarily the following:

- Replacing the existing organisation, structured mainly according to the value chain in the respective geographic regions, by a functionally led organisation structured in cross-border Business Divisions and Business Units;
 - A number of functional areas have been identified. Responsibility for these is delegated to cross-border Staff Functions, which take over for the former functions at the Group level as well as the Business Group and Business Unit levels;
 - Establishment of a Group-wide Shared Service unit.
- The organisational chart that applies from 1 January 2011 is illustrated on page 69.

In autumn 2010 an extensive project was carried out to prepare for implementation of the new organisation. Part of this project also involved increased process orientation and updating the Vattenfall Management System, and reshaping it into a more effective tool for governance. This project continues until the second quarter of 2011 (throughout 2011 for the VMS) and focuses particularly on organisation and governance, finance, personnel matters, functional areas, shared services, systems and on the transition to the new organisational structure.

Internal control of the financial reporting

This report has been prepared in accordance with the Swedish Code of Corporate Governance.

Control environment

The formal decision-making structure in the Group is based on the division of responsibility between the Board and CEO, which is laid forth in the Board's Rules of Procedure. The Board has established Vattenfall's Group-wide Code of Conduct, which defines the obligation of all employees to adhere to Vattenfall's company philosophy, Code of Conduct, core values, and norms for the employees. The Vattenfall Management System (VMS), which has been established by the CEO, contains governing documents that include, among other things, Group instructions for authorisations, governance, risk management and internal control.

Vattenfall applies the "three lines of defence" model, in accordance with the Basel II recommendations, where management and control of risks are divided into three lines of defence. The first line of defence consists of the Business units, which own and manage risks. The risk organisation makes up the second line of defence and is responsible for monitoring risks. The auditor and the internal auditor is the third line of defence and performs an independent review and oversight of both the first and second lines of defence.

Risk analysis

The rules and outcome of the Group's risk assessment and risk management processes are reviewed by the Board each year. The Group's risk management and reporting are coordinated by a central risk committee. The Board evaluates and monitors risks and the quality of financial reporting via the Audit Committee, which maintains continuous and regular contact with the Group's internal and external audit functions in order to evaluate risk in the financial reporting. The VMS includes a framework for internal control that identifies and defines material risks related to financial reporting. The Finance Compliance function within the Staff function finance performs yearly analyses of risks related to financial reporting and is responsible for updating this framework.

Control activities and follow-up

The Board monitors the Parent Company's and Group's financial position and addresses this matter at every ordinary board meeting. The EGM has regular follow-up meetings on the financial outcome with the management and finance functions of Vattenfall's various Business Divisions, Staff functions and Shared Service Units. The VMS contains governing documents for the essential financial reporting processes. The VMS serves as a platform for internal control for all units within the Group.

The Finance Compliance function is responsible for overseeing self assessments, follow-up, reporting and improvements in the control activities for financial reporting. These control activities are intended to prevent, discover and correct errors in the financial reporting. The Finance Compliance function reports to Vattenfall's CFO and Audit Committee.

Internal Audit's work involves, among other things, evaluating and reviewing risk management, compliance with policies, rules and instructions, and the effectiveness of internal control in the financial reporting. Internal Audit reports to the Executive Group Management, to the management teams in the various countries and units, and to Vattenfall's Audit Committee.

Information and communication

Information about the Group's policies, instructions, guidelines and manuals is posted on Vattenfall's intranet, which is accessible to all employees in the Group. The Group's accounting and reporting policies are laid out in the Group reporting manual. Updates and changes of these policies are communicated on a continuous basis via Vattenfall's intranet as well as at meetings with representatives of Vattenfall's Business Divisions, Staff functions and Shared Service units.