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TOMORROW

Danfoss

Statutory report on corporate governance

under Section 107b of
the Danish Financial Statements Act



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Statutory report on corporate governance

under Section 107b of the Danish Financial Statements Act

Section 107b of the Danish Financial Statements Act requires listed companies to disclose whether they are covered by a code on corporate governance (subsections 1-5). They are also required to describe in their financial reporting the main elements of their internal risk management and controls systems (subsection 6) as well as the composition of their management functions and committees (subsection 7).

Danfoss filed in November 2014 a Euro Medium Term Program on the Irish Stock Exchange and is therefore as of that date considered a class D company with listed bonds. Danfoss only has to comply with the rule set out in section 107b, section 1, no 6 of the Danish Financial Statements Act applying to companies with listed bonds, including the exceptions regarding issuers of bonds above EUR 100,000. The statutory report on corporate governance at Danfoss A/S forms a part of the Management Report provided in the Danfoss Annual Report 2015, covering the accounting period of January 1 - December 31, 2015. (Reference is also made to page 9 for further clarification).

As its code of corporate governance, Danfoss follows the recommendations on corporate governance as set out by the Committee on Corporate Governance in Denmark. Danfoss has taken a 'comply or explain' approach to the recommendations and regularly assesses how the Group can further improve its compliance with them. With a few exceptions, Danfoss complies with these recommendations, which are available on: www.corporategovernance.dk, the website of the Committee on Corporate Governance. The section on the code of corporate governance, which is found at the end of this document, is not covered by the independent auditors'

report provided in Danfoss' Annual Report. Information about the company's control and risk management systems and the composition of the company's management bodies etc. is covered by the independent auditors' report provided in Danfoss' Annual Report.

Statement of internal control and risk management systems in the financial reporting process

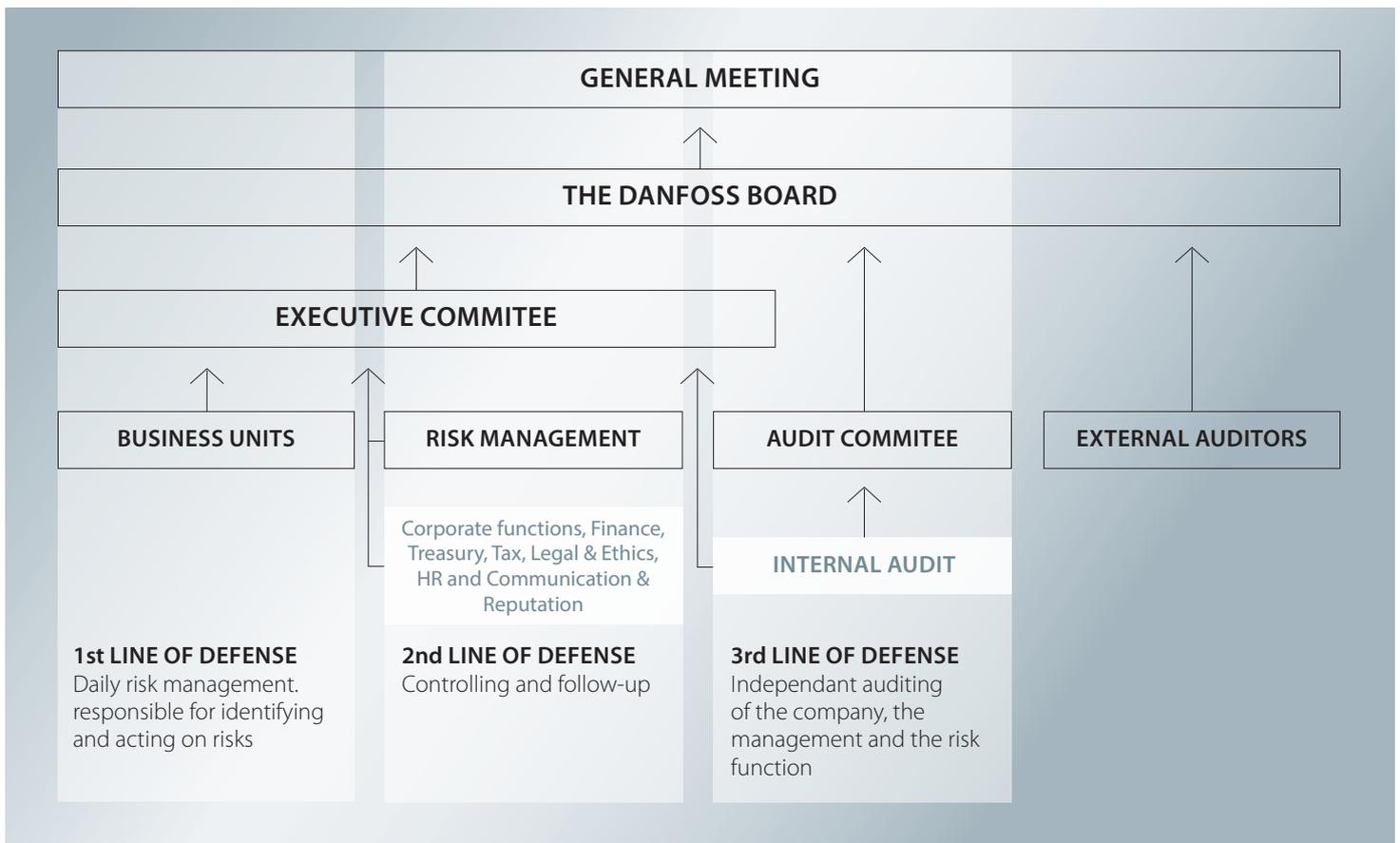
Danfoss' consolidated financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS) and Danish disclosure requirements as set out in the Danish Financial Statements Act. Danfoss has set up internal control and risk management systems to ensure that its financial reporting complies with the above-mentioned rules.

The internal control and risk management systems are divided into the following categories:

- Control environment
- Risk assessment
- Control structure
- Information and communication
- Monitoring

Control environment

Danfoss has a two-tier management system consisting of a Board of Directors and an Executive Committee. The Danfoss Board of Directors and the Executive Committee have the overall responsibility for the Group's risk management and internal controls in its financial reporting, including the responsibility for the Group's compliance with all relevant legislation and regulations in connection with the financial reporting. Furthermore, corporate governance in Danfoss is



based on Danish law and the company's Articles of Association, corporate values and a large number of internal management and control procedures.

The Board of Directors and the Executive Committee establish and approve the overall policies, procedures and controls in relation to significant parts in the financial reporting process, including, among other things, IT, tax matters and accounting estimates. The Executive Committee is responsible for compliance with policies and procedures, whereas the relevant functions and areas are responsible for following them. Enforcement of the policies and procedures is based on clear principles for delegation of responsibility, including clear reporting structures, authorization and validation procedures as well as the explicit division of responsibilities.

The most significant policies, manuals and procedures in relation to financial reporting include: an accounting and reporting manual (containing minimum requirements for business procedures, internal controls, segregation of duties, reconciliations, approvals, authorization, validation, accounting policies, internal and external reporting, etc.), a treasury and finance policy, including counterparty approval, determining financial transaction and counterparty lines and limits, a tax policy, an IT strategy, and an IT security policy, an ethics handbook and a whistleblower function for reporting of unethical conduct. The adopted policies, manuals and procedures are available on the Group's intranet, and the company stresses on a regular basis the need to comply with them, in part by means of e-learning. Danfoss continuously monitors compliance with policies and procedures, performing random checks through its internal audit function and otherwise.

The purpose of the control activities is to prevent, detect and correct any errors or irregularities as well as ensuring that applied estimates are reasonable under the circumstances. In order to ensure efficient controls, Danfoss applies three lines of defense. The business units' own self-control constitutes the first line of defense. Danfoss' control functions, including the Group's controlling and compliance functions, constitute the second line of defense and the internal audit function, which reports directly to the Board's audit committee, constitutes the third line of defense. The internal control functions also monitor the use of IT and tax matters.

The Executive Committee oversees that relevant legislation and other instructions and provisions applying to the financial reporting are complied with and reports on this on an ongoing basis to the Board's audit committee, which is constituted by the entire Board. The audit committee met four times in 2015.

Risk assessment

A number of items in the annual report are based on estimates or similar assessments, which increase the risk of errors in these items compared to other items in the financial statements. Note 27 "Critical accounting estimates and judgements" in the annual report sets out the areas which pose the most significant risks of misjudgment.

The Executive Committee and the audit committee evaluate, on an ongoing basis, risks considered to have a potential impact on the Group's financial reporting. Evaluations are performed at, for instance, quarterly business review meetings between the Executive Committee and each segment unit. The risks are

treated according to their potential impact and the probability of them materializing.

At least once a year, the Board's audit committee and the Executive Committee perform a general assessment of risks related to the financial reporting. As part of this process, they assess the risk of fraud and the measures needed to mitigate or eliminate such risks. The assessment also includes the risk of the day-to-day management disregarding controls and exerting undue influence on the financial reporting.

A detailed description of general risk management at Danfoss is provided in Danfoss' Annual Report 2015, in the section on Risk Management and Compliance.

Control structure

Danfoss' corporate standards describe the requirements that apply to the accounting systems. Those standards are revised and improved as and when considered necessary. The Group's subsidiaries report financial information for use in the Annual Report and in quarterly reports in a shared reporting environment. The reporting by the subsidiaries is checked on an ongoing basis and procedures have been set up to ensure that any errors or inadequacies in the data reported are communicated to and corrected by the subsidiaries.

The reporting is prepared in accordance with IFRS (International Financial Reporting Standards).

Danfoss' standards pertaining to accounting and controls have been prepared so as to create uniform and reliable reporting which uphold the quality of the Group financial statements. Group Controlling supervises and checks that reports comply with corporate standards. Moreover, the internal audit function performs random checks on the reporting as well as on the controlling process to minimize the risk of fraud and misreporting.

Information and communication

Danfoss' corporate standards for financial reporting are available to all employees on the Group's intranet. Additional policies, guidelines and instructions can be found on the Corporate Finance intranet site.

In addition, Danfoss ensures that all reporting responsibilities are updated regularly on changes to legislation and regulations, using written means of communication such as e-mail. Danfoss has also established a Finance Board, where the segment heads of finance and Danfoss' Chief Financial Officer liaise to discuss and communicate important financial and reporting issues. The Danfoss Finance Board meets 6-12 times per year.

Monitoring

Danfoss has a two-tier internal control system which divides the responsibility for monitoring and mitigating financial risks between the central corporate functions on the one hand and the business units on the other. The business units monitor the transactions from a business perspective, whereas the central corporate functions monitor the transactions from a legal perspective.

Danfoss' controlling function performs a series of controls, recurring as well as ad hoc, to monitor subsidiaries' financial reporting. These controls also include financing and tax reporting matters. Each month, Group management receives a report on issues identified in the most recent monthly reporting. In addition, the internal audit function performs a series of inspection visits to audit selected companies' compliance with Danfoss' standards around IT, internal control systems and procedures, as well as compliance with legislation and regulations. On a regular basis, the issues identified during inspection visits to the subsidiaries are reported to the Executive Committee.

Tax- and duty-related issues are furthermore subject to a two-tier control system where the individual business units are responsible for the local tax and duty matters and the reporting on these. The central corporate tax function handles affairs relating to the Parent Company and supervises the subsidiaries. This is achieved through implementation of processes, random checks and validation in connection with reporting.

Composition of company management bodies

Danfoss has a two-tier management system consisting of a Board of Directors and an executive committee. The Board of Directors is elected by the Danfoss shareholders at the annual general meeting, with the exception of employee representatives, who are elected by the employees for four-year terms. The Board of Directors appoints and supervises the Executive Committee which has overall responsibility for the day-to-day operations of the company and delegates areas of responsibility and decision-making powers to the company's business units and corporate functions in accordance with current guidelines and legislation.

Annual general meetings

The annual general meeting is the supreme authority in all company matters. General meetings are called by the Board of Directors at not less than two weeks and not more than four weeks' notice by an announcement inserted in a national newspaper as determined by the Board of Directors and by ordinary letter to all registered shareholders having so requested. The announcement must include the agenda of the general meeting. All shareholders are entitled to attend general meetings, provided they have requested an admission card, against providing appropriate identification, not later than three days prior to the general meeting from an address specified in the notice.

To be considered at annual general meetings, proposals from shareholders must be submitted to the Board of Directors no later than six weeks before the annual general meeting. Danfoss has both class A and class B shares. Class A shares carry ten votes each, while class B shares carry one vote each. Resolutions are passed by simple majority of voters at general meetings, unless otherwise provided by legislation or Danfoss' Articles of Association.

The Board of Directors

The Board of Directors is elected by the shareholders at the general meeting and has the overall responsibility for the company's activities. Shareholder-elected Board members are elected for the term until the following year's annual general

Composition of the board of directors ¹⁾

| | Nationality | Independent | Audit Committee |
|-----------------------------------|-------------|-------------|-----------------|
| Jørgen Mads Clausen (Chairman) | DK | No | ● |
| Mads-Peter Clausen | DK | No | ● |
| Jürgen Reinert | DE | Yes | ● |
| William Ervin Hoover | US | Yes | ● |
| Kasper Rørsted | DK | Yes | ● |
| Björn Rosengren | SE | Yes | ● |
| Lars Grau ²⁾ | DK | - | ● |
| Jens Peter Nielsen ²⁾ | DK | - | ● |
| Sandra N. Bertelsen ²⁾ | DK | - | ● |

¹⁾ From the Annual General Meeting held in April 2015 to the 2016 Annual General Meeting

²⁾ Elected by the employees

● Chairman of the Audit Committee

meeting to the effect that all shareholder-elected members may stand for re-election at each annual general meeting. Pursuant to Danish legislation, employee representatives serve on the Board for terms of four years and may stand for re-election. The Board appoints a chairman and one or two vice-chairmen from among its members.

All appointments are for terms of one year.

The Board of Directors approves the overall strategies and objectives of the company as developed and proposed by the Executive Committee. The Board of Directors also defines the guidelines for the Executive Committee on its day-to-day operation of Danfoss. The distribution of tasks between the Board of Directors and the Executive Committee is set out in the rules of procedure, which are reviewed on an ongoing basis. Matters discussed at Board meetings are decided by a simple majority of votes.

In the event of an equality of votes, the Chairman has the casting vote. At least five Board meetings are held each year, one of which is held in connection with a visit to one of the Group's sites. The Board of Directors reviews and approves the Group's strategy (perspective plan) and targets.

The Executive Committee normally attends Board meetings, unless the Board is reviewing matters pertaining to the Executive Committee.

Rules concerning the recruitment of new shareholder-elected Board members

It is important to Danfoss to have a dynamic and professional Board whose members possess the knowledge and experience necessary to ensure the Group's long-term performance. When searching for new members, the Board of Directors considers a candidate's qualifications relative to how they match the company's needs and the combined qualifications and general composition of the Board overall.

Rules for the election of employee-representatives to the Board

Pursuant to the Danish Companies Act, employees in Denmark are entitled to elect a number of members and alternates to the Board (at least two members), corresponding to half the number of shareholder-elected Board members. Accordingly, employees at Danfoss have elected three representatives from among their colleagues to serve on the Board.

The most recent election of employee-representatives to the Board was held in January 2014, in a secret ballot. The election took effect as of the annual general meeting held in April 2014. The next election takes place in 2018. Employee-elected Board members serve for terms of four years. Eligible candidates must be of legal age and have been employed for a full year prior to the election. If a member ceases to be employed by Danfoss, he or she must resign from the Board.

The employee-elected Board members have the same rights, obligations and responsibilities as shareholder-elected Board members.

Audit Committee

Since January 1, 2009, listed companies in Denmark have been required to have an audit committee. The Danfoss Board has opted to comply with the regulations and set up an audit committee in 2010. The rules provide that the tasks, responsibilities and authority of the audit committee may be organized in an independent committee or be performed by the entire Board. At Danfoss, the entire Board performs the function of the audit committee. In connection with Board meetings, the Board also holds audit committee meetings.

The main objectives of the audit committee are to:

- Monitor the financial reporting process (reliable reporting)
- Supervise the efficiency of the company's internal control system and risk management systems
- Monitor the statutory audit of the financial statements, etc.

- Monitor and verify the auditors' independence, cf. Section 24 of the Danish Act on State-authorized and Registered Public Accountants, including, in particular, the provision of additional services to the company
- Monitor the external auditors' competencies and findings
- Make recommendations to the Board regarding the appointment of auditors.

Internal audit

At the beginning of 2011, Danfoss decided to set up an internal audit function to carry out independent internal checks. The internal audit function will submit its findings to the audit committee.

Executive Committee

The Executive Committee, consisting of from two to six members, has the day-to-day responsibility for Danfoss' operations and is appointed by the Board of Directors. In 2015, the Executive Committee consisted of:



Niels Bjørn Christiansen
President & CEO



Kim Fausing
Executive Vice President & COO



Jesper V. Christensen
Executive Vice President & CFO

The current age limit for Executive Committee members is 70. The Executive Committee holds formal meetings once a week. According to the rules of procedure, the Executive Committee must ensure that the following issues are addressed at Board meetings at least once a year:

- An assessment of internal control functions, including IT security
- Capital resources, book-keeping, asset management and accounting function
- Risk management systems, including insurance matters and currency management
- A review of the rules of procedure
- Corporate governance and internal codes of practice
- The preparation of budgets and perspective plans (three-year plans)

The Executive Committee is supported by a number of corporate functions, including: Communications & Reputation, Corporate Finance, Legal, M&A, Ethics and Compliance and HR.

Danfoss Leadership Team

The Danfoss Leadership Team consists of the Executive Committee and, the four Segment Presidents as well as the Senior Vice President of Communications & Reputation, the Senior Vice President of HR and the Senior Vice President of Danfoss Group IT.

Corporate governance recommendations

The Committee on Corporate Governance in Denmark has defined a series of recommendations on corporate governance, which now form part of the rules for companies listed on NASDAQ OMX Copenhagen. Danfoss is a family- and foundation-owned company and has bonds listed at the Irish Stock Exchange, and is as such, not subject to the same disclosure requirements as companies with listed shares.

The Group has, with a few exceptions, opted to follow the guidelines that apply to publicly-traded companies. Danfoss' approach to the recommendations is based on the 'comply or explain' principle and the group assesses on an ongoing basis the possibilities of further improving its compliance with the recommendations. The recommendations refer to the Executive Committee as 'the central governing body', whereas 'the supreme governing body' refers to the Board of Directors.

The chart below includes both a list of the Recommendations on Corporate Governance and Danfoss' stance on those recommendations.

| RECOMMENDATION | THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON: | |
|---|---|--|
| 1 The company's communications and interaction with its investors and other stakeholders | | |
| 1.1. Dialogue between the company, the shareholders and other stakeholders | | |
| <p>1.1.1. The Committee recommends that the Board of Directors ensure ongoing dialogue between the company and its shareholders in order for the shareholders to gain relevant insight into the company's potential and policies, and in order for the Board of Directors to be aware of the shareholders' views, interests and opinions on the company.</p> |  | <p>As a family- and foundation-owned company, Danfoss does not have the same need to engage with all shareholders on a daily basis as a listed company does. Danfoss maintains close contact with the Bitten and Mads Clausen Foundation and the Clausen family, the two largest shareholders of Danfoss A/S. Furthermore, representatives of the largest shareholders are members of the Danfoss A/S Board of Directors.</p> |
| <p>1.1.2. The Committee recommends that the Board of Directors adopts policies on the company's relationship with its stakeholders, including shareholders and other investors, and that the Board ensures that the interests of the stakeholders are respected in accordance with company policies.</p> |  | <p>Danfoss has policies concerning the company's relationship with its stakeholders. Information about Danfoss and Danfoss policies are available to shareholders and other stakeholders on the company's website.</p> |
| <p>1.1.3. The Committee recommends that the company publish quarterly reports.</p> |  | <p>Danfoss releases quarterly announcements.</p> |
| 1.2. Annual General Meeting | | |
| <p>1.2.1. The Committee recommends that, when organizing the company's general meeting, the Board of Directors plans the meeting to support active ownership.</p> |  | <p>Danfoss engages actively with the shareholders at the company's annual general meeting. Danfoss convenes annual general meetings via the company's intranet, Danish newspapers and via Danfoss' internal employee magazine. On the intranet and via the internal employee magazine, shareholders are invited to submit proposals to be considered at the annual general meeting. The Annual Report, the agenda and other documents are available for inspection at the company's offices and on the Danfoss internet before the annual general meeting.</p> |
| <p>1.2.2. The Committee recommends that proxies granted for the general meeting allow shareholders to consider each individual item on the agenda.</p> |  | <p>Shareholders mainly execute their voting right in person. Shareholders wishing to issue a proxy to the Board of Directors may do so, but proxy documents are not forwarded to all shareholders in connection with annual general meetings. Proxy documents are forwarded to those shareholders who so request.</p> |
| 1.3. Takeover bids | | |
| <p>1.3.1. The Committee recommends that the company set up contingency procedures in the event of takeover bids from the time that the Board of Directors has reason to believe that a takeover bid will be made. According to such contingency procedures, the Board of Directors should not without the acceptance of the general meeting, attempt to counter the takeover bid by making decisions which in reality prevent the shareholders from deciding on the takeover bid themselves.</p> |  | <p>Due to Danfoss' ownership structure, the Board of Directors does not find it necessary to establish such procedures.</p> |

| RECOMMENDATION | | THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON: |
|--|---|--|
| 2. The tasks and responsibilities of the Board of Directors 2.1. Overall tasks and responsibilities | | |
| 2.1.1. The Committee recommends that at least once a year the Board of Directors takes a position on the matters related to the Board's performance of its responsibilities. |  | The Board of Directors continuously determines its tasks on the basis of Danfoss' current needs – also in cooperation with the Executive Committee. Furthermore, to be in line with Danfoss' strategy etc., it is considered how to ensure the most optimal composition of the Board. |
| 2.1.2. The Committee recommends that at least once a year the Board of Directors takes a position on the overall strategy of the company with a view to ensuring value creation in the company. |  | The Executive Committee presents Danfoss' overall strategy once every year, and reviews the strategy of each Business Area together with the Board on an ongoing basis. |
| 2.1.3. The Committee recommends that the Board of Directors ensures that the company has a capital and share structure ensuring that the strategy and long-term value creation of the company are in the best interest of the shareholders and the company, and that the Board of Directors presents this in the management commentary on the company's annual report and/or on the company's website. |  | The Board of Directors evaluates on an ongoing basis whether Danfoss' capital and share structures continue to be appropriate, and it considers the present structure to be appropriate. Danfoss' Articles of Association stipulate that the shares are divided into A- and B-shares, with A-shares carrying ten votes and B-shares carrying one vote. A- and B-shares have the same denomination (DKK 100). Other than this, no shares carry special rights. The Bitten and Mads Clausen Foundation owns A-shares with a total nominal value of DKK 405m (of which DKK 400m forms part of the original share capital, for which reason the Foundation is not in a position to sell those shares) and B-shares of DKK 104m nominal value (forming part of the disposable capital). Accordingly, the Foundation controls about 85% of the votes in Danfoss A/S. This is consistent with the objects clause of the Bitten and Mads Clausen Foundation. The charter of the Bitten and Mads Clausen Foundation provides that the foundation Board has the right to abolish the share classes if Danfoss A/S is listed. As long as Danfoss is not listed, the share classes will remain unchanged, which the Board considers to be in the best interest of the shareholders and the company. |
| 2.1.4. The Committee recommends that the Board of Directors annually review and approve guidelines for the Executive Board; this includes establishing requirements for the Executive Board on timely, accurate and adequate reporting to the Board of Directors. |  | As a minimum, the rules of procedure are reviewed once a year and updated as necessary. |
| 2.1.5. The Committee recommends that at least once a year the Board of Directors discusses the composition of the executive Board, as well as developments, risks and succession plans. |  | At least once a year the Board of Directors discusses the Executive Committee's composition, including succession plans, development activities and competences. |

| RECOMMENDATION | | THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON: |
|--|---|--|
| <p>2.1.6. The Committee recommends that once a year the Board of Directors discusses the company's activities to ensure relevant diversity at management levels, including setting specific goals and accounting for its objectives and progress made in achieving the objectives in the management commentary on the company's annual report and/or on the website of the company.</p> |  | <p>Danfoss has prepared policies and identified target figures concerning diversity in the company's management levels. The policy is available on Danfoss' website.</p> |
| <p>2.2. Corporate social responsibility</p> | | |
| <p>2.2.1. The Committee recommends that the Board of Directors adopts policies on corporate social responsibility.</p> |  | <p>Danfoss has adopted policies on corporate social responsibility and reports on its social, environmental and ethical efforts on an ongoing basis.</p> |
| <p>2.3. The Chairman and Vice-Chairman of the Board of Directors</p> | | |
| <p>2.3.1. The Committee recommends appointing a Vice-Chairman of the Board of Directors who will assume the responsibilities of the Chairman in the event - of the Chairman's absence, and who will also act as an effective sparring partner for the chairman.</p> |  | <p>Immediately following the annual general meeting, the Board convenes to elect a Chairman and a Vice-Chairman among its members.</p> |
| <p>2.3.2. The Committee recommends ensuring that, if the Board of Directors in exceptional cases, asks the chairman of the Board of Directors to perform special operating activities for the company, including briefly participating in the day-to-day management, a Board resolution to that effect be passed and precautions taken to ensure that the Board of Directors maintains its independent, overall management and control function. Resolutions on the chairman's participation in the day-to-day management and the expected duration hereof should be published in a company announcement.</p> |  | <p>The Chairman of the Board does not take part in the day-to-day management and does not perform special tasks on behalf of the company other than carrying out the duties as Chairman of the Board. If the Chairman of the Board is asked to perform special tasks, the Board will comply with the recommendation.</p> |

RECOMMENDATION

THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON:

3. Composition and organization of the Board of Directors

3.1. Composition

3.1.1.

The Committee recommends that the Board of Directors annually accounts for:

- the skills it must have to best perform its tasks,
- the composition of the Board of Directors, and
- the special skills of each member.



Danfoss finds it important to have a dynamic and professional Board whose members possess the knowledge and experience necessary to ensure the Group's long-term growth. The Board does not believe that the specific requirements of Board members' qualifications should be set out in advance, because this would imply a risk of excluding candidates who do not fully meet the requirements.

3.1.2.

The Committee recommends that the selection and nomination of candidates for the Board of Directors be carried out through a thoroughly transparent process approved by the overall Board of Directors. When assessing its composition and nominating new candidates, the Board of Directors must take into consideration the need for integration of new talent and diversity in relation to age, international experience and gender.



When searching for new Board members, the Board of Directors considers a candidate's qualifications relative to how they match the company's needs and the combined qualifications and general composition of the Board overall, but no formal procedure to this effect has been defined. Candidates for the Board are elected upon discussions with the Board of the Bitten and Mads Clausen Foundation, because the Foundation has the voting majority in Danfoss A/S. The company considers this to be the best process in light of the distribution of votes among the shareholders.

3.1.3.

The committee recommends that the notice convening the general meeting when election of members to the board of directors is on the agenda be accompanied by a description of the nominated candidates' qualifications, including information about the candidates'

- other executive functions, among these memberships in executive boards, boards of directors, and supervisory boards, including board committees in foreign enterprises
- demanding organisational tasks,
- and information about whether candidates to the board of directors are considered independent.



Danfoss presents the final shortlist of candidates for the Board for review at the annual general meeting. A more detailed presentation of each candidate is provided at the annual general meeting.

3.1.4.

The Committee recommends that the company's articles of association stipulate a retirement age for members of the Board of Directors.



The age limit for Board members is 70, cf. Section 7 in the Articles of Association. Information about the age limit and the age and length of service of each Board member is available in the Annual Report.

3.1.5.

The Committee recommends that the members of the Board of Directors are up for election every year at the annual general meeting.



The members of the Board of Directors are elected by the annual general meeting for the period until the next annual general meeting.

RECOMMENDATION

THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON:

3.2. The independence of the Board of Directors

3.2.1.

In order for the members of the Board of Directors to act independently of special interests, the Committee recommends that at least half of the members of the Board of Directors elected by the general meeting be independent persons, in order for the Board of Directors to be able to act independently of special interests.

To be considered independent, this person may not:

- Be or within the last five years have been a member of the executive Board, or senior staff member in the company, or an associate
- Within the past five years, have received larger emoluments from the company/group, a subsidiary undertaking or an associate in another capacity than as member of the Board of Directors
- Represent the interests of a controlling shareholder
- Within the past year, have had significant business relations (e.g. personal or indirectly as partner or employee, shareholder, customer, supplier or member of the executive management in companies with corresponding connection) with the company, a subsidiary undertaking or an associate
- Be or within the past three years have been, employed or partner at the external auditor
- Have been chief executive in a company holding cross-memberships with the company
- Have been a member of the Board of Directors for more than 12 years, or
- Have close relations with persons who are not considered independent persons



Of the six members elected by the annual general meeting, four are considered to be independent.

3.3. Board members and the number of other executive functions

3.3.1.

The Committee recommends that each member of the Board of Directors assesses the expected time commitment for each function in order that the member does not take on more functions than s/he can manage satisfactorily for the company.



Each member individually assesses whether his/her different commitments allow him/her to satisfactorily perform his/her duties in the Board.

| RECOMMENDATION | | THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON: |
|--|---|---|
| <p>3.3.2. The Committee recommends that the management commentary, in addition to the provisions laid down by legislation, includes the following information about the members of the Board of Directors:</p> <ul style="list-style-type: none"> • Position of the relevant person • Age and gender of the relevant person • Whether the member is considered independent • Date of appointment to the Board of Directors of the member • Expiry of the current election period • Other executive functions, e.g. memberships in executive Boards, Boards of Directors and supervisory Boards, including Board committees, in foreign enterprises and • Demanding organizational tasks, and • Number of shares, options, warrants and similar in the company and other group companies of the company, owned by the member, as well as changes in the portfolio of the member of the securities mentioned which have occurred during the financial year. |  | <p>Danfoss provides – both on its website and in the annual report – information about each Board member’s age, year of joining the Board, position, other Board functions, corporate positions and other executive functions. Danfoss does not state the number of shares held by individual Board members, but candidates standing for election to the Board at the annual general meeting are classified as independent or not independent.</p> |
| <p>3.4. Management Boards (or committees)</p> | | |
| <p>3.4.1. The Committee recommends that the company publish the following on the company’s website:</p> <ul style="list-style-type: none"> • The terms of reference of the Board committees, • Most important activities of the committees during the year, and the number of meetings held by each committee, and • Names of the members of each committee, including the chairmen of the committees, as well as information on which members are independent members and which members have special qualifications. |  | <p>Danfoss set up an audit committee in 2011. The duties and responsibilities of the audit committee as well as its authority can either be organized in an independent body or be executed by the entire Board. At Danfoss, the entire Board performs the function of the audit committee. The Board consists of six members, four of which are considered to be independent. The activities and tasks of the audit committee are set out in the committee’s terms of reference. Information about the number of committee meetings is available on the Danfoss website and in the annual report. The committee is headed by William Ervin Hoover.</p> |
| <p>3.4.2. The Committee recommends that a majority of the members of a Board committee be independent.</p> |  | <p>Of six members elected at the General Assembly, four are independent.</p> |
| <p>3.4.3. The Committee recommends that the Board of Directors sets up a formal audit committee composed such that</p> <ul style="list-style-type: none"> • The chairman of the Board of Directors is not chairman of the audit committee, and • Between them, the members should possess such an expertise and experience as to provide an updated insight into and experience in the financial, accounting and audit aspects of companies whose shares are admitted to trading on a regulated market. |  | <p>At Danfoss, the entire Board performs the function of the audit committee. The Board believes that the aggregate expertise and experience of the audit committee members constitute an updated insight into and experience of financial matters as well as accounting and audit issues pertaining to the Group. The chairman of the audit committee is William Ervin Hoover. For information about William Ervin Hoover’s qualifications, go to www.danfoss.com.</p> |
| <p>3.4.4. The Committee recommends that, prior to the approval of the annual report and other financial reports, the audit committee monitors and reports to the Board of Directors about:</p> <ul style="list-style-type: none"> • Significant accounting policies, • Significant accounting estimates, • Related party transactions, and • Uncertainties and risks, including in relation to the outlook for the current year. |  | <p>The Danfoss Board has always monitored and reviewed the accounting policies, accounting estimates, related party transactions as well as risks and uncertainties, including in respect of the company’s outlook.</p> <p>Since January 1, 2011, these tasks have been undertaken by the audit committee.</p> |

| RECOMMENDATION | | THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON: |
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| <p>3.4.5. The Committee recommends that the audit committee:</p> <ul style="list-style-type: none"> • Annually assesses the need for an internal audit, and in such case, makes recommendations on selecting, appointing and removing the head of the internal audit function and on the budget of the internal audit function, and • Monitor the executive Board’s follow-up on the conclusions and recommendations of the internal audit function. |  | <p>Danfoss has set up an internal audit function, which reports to the audit committee (with staff reference to Danfoss’ CFO).</p> |
| <p>3.4.6. The Committee recommends that the Board of Directors establishes a nomination committee chaired by the chairman of the Board of Directors with at least the following preparatory tasks:</p> <ul style="list-style-type: none"> • Describe the qualifications required by the Board of Directors and the executive Board, and for a specific membership, state the time expected to be spent on having to carry out the membership, as well as assess the competences, knowledge and experience of the two governing bodies combined • Annually assess the structure, size, composition and results of the Board of Directors and the executive Board, as well recommend any changes to the Board of Directors • Annually assess the competences, knowledge and experience of the individual members of the management, and report to the Board of Directors in this respect • Consider proposals from relevant persons, including shareholders and members of the Board of Directors and the executive Board for candidates for the Board of Directors and the executive Board, and • Propose an action plan to the Board of Directors on the future composition of the Board of Directors, including proposals for specific changes |  | <p>Danfoss has decided not to set up a nomination committee. Instead, the entire Board handles this task.</p> |
| <p>3.4.7. The Committee recommends that the Board of Directors establishes a remuneration committee with at least the following preparatory tasks:</p> <ul style="list-style-type: none"> • To recommend the remuneration policy (including the general guidelines for incentive-based remuneration) to the Board of Directors and the executive Board for approval by the Board of Directors prior to approval by the general meeting, • Make proposals to the Board of Directors on remuneration for members of the Board of Directors and the executive Board, as well as ensure that the remuneration is in compliance with the company’s remuneration policy and the assessment of the performance of the persons concerned. The committee should have information about the total amount of remuneration that members of the Board of Directors and the executive Board receive from other companies in the group, and • Recommend a remuneration policy applicable for the company |  | <p>Danfoss has decided not to set up a remuneration committee. Instead, the Board handles this task. The Chairman and Vice-Chairman assess and determine annually the remuneration to be paid to Board members and the Executive Committee and submit the remunerations to the Board of Directors for approval.</p> |

| RECOMMENDATION | | THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON: |
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| <p>3.4.8. The Committee recommends that the remuneration committee does not consult with the same external advisers as the executive Board of the company.</p> |  | <p>A remuneration committee has not been established.</p> |
| <p>3.5. Management Boards (or committees) Evaluation of the performance of the Board of Directors and the Executive Committee</p> | | |
| <p>3.5.1. The Committee recommends that the Board of Directors establishes an evaluation procedure where contributions and results of the Board of Directors and the individual members, as well as cooperation with the executive Board are annually evaluated. Significant changes deriving from the evaluation should be included in the management commentary or on the company's website.</p> |  | <p>Danfoss introduced a formal annual evaluation process in 2012.</p> |
| <p>3.5.2. The Committee recommends that, in connection with the preparation of the general meeting, the Board of Directors considers whether the number of members is appropriate in relation to the requirements of the company. This should help ensure a constructive debate and an efficient decision-making process in which all members are given the opportunity to participate actively.</p> |  | <p>Danfoss introduced a formal annual evaluation process in 2012. When evaluating the performance, the individual Board members are also asked if they consider the composition of the Board – including the number of Board members – satisfactory.</p> |
| <p>3.5.3. The Committee recommends that at least once every year the Board of Directors evaluates the work and performance of the executive Board in accordance with pre-defined clear criteria.</p> |  | <p>The Board evaluates the Executive Committee's work on an ongoing basis, but an evaluation has not yet been performed using set criteria because the Board finds it more appropriate to evaluate the work as any current challenges arise.</p> |
| <p>3.5.4. The Committee recommends that the executive Board and the Board of Directors establishes a procedure according to which their cooperation is evaluated annually through a formalized dialogue between the chairman of the Board of Directors and the chief executive officer and that the outcome of the evaluation is presented to the Board of Directors.</p> |  | <p>The cooperation between the Board and the Executive Committee is evaluated on an ongoing basis, and the Executive Committee has an ongoing dialogue with the chairman, who keeps the Board updated on these discussions. An annual evaluation is therefore not performed.</p> |

RECOMMENDATION

THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON:

4 Remuneration of members of the governing bodies

4.1. Content and form of the remuneration policy

4.1.1.

The Committee recommends that the Board of Directors prepares a clear and transparent remuneration policy applicable for the Board of Directors and the executive Board including

- A detailed description of the components of the remuneration for members of the Board of Directors and the executive Board
- The reasons for choosing the individual components of the remuneration, and
- A description of the criteria on which the balance between the individual components of the remuneration is based.

The remuneration policy must be approved by the general meeting and published on the company's website.



The Board of Directors has adopted a remuneration policy for the Board of Directors and the Executive Committee.

The remuneration policy sets out in detail the components of the overall remuneration.

The Board members are paid an annual fee which is determined at the annual general meeting. In addition, some of the Board members can be paid a fee for the performance of special duties, including as chairman of Board committees. The Executive Committee members have individual remuneration schemes which are adjusted once a year by the Chairman. The Executive Committee is paid a remuneration package consisting of three components: the gross salary, which includes a company pension contribution, and a bonus plan, which relates to bonus targets for the current financial year as well as long-term targets. Share options have previously been allotted, but the company does not use share option schemes any more.

Members of the Executive Committee may choose to retire at the age of 60 and their term of notice is 12 months. The members of the Executive Committee are entitled to severance pay amounting to 24 months' pay, if their employment is terminated for reasons other than their own resignation. The CEO of the company is entitled to severance pay and can resign at short notice in the event that Danfoss is taken over by another company.

The remuneration policy is available on Danfoss' website. The motivation for the individual components of the remuneration package and a presentation of how each component is weighted is provided at the annual general meeting in connection with the approval of the remuneration policy.

4.1.2.

The Committee recommends that, if the remuneration policy includes variable components,

- Limits be set on the variable components of the total remuneration package
- A reasonable and balanced linkage be ensured between remuneration for governing body members, expected risks and the value creation for shareholders in the short and long terms
- There be clarity about performance criteria and measurability for award of variable components
- There be criteria ensuring that qualifying periods for variable components in remuneration agreements are longer than one calendar year, and
- An agreement is made which, in exceptional cases, entitles the company should be able to reclaim in full or in part variable components of remuneration that were paid on the basis of data, which proved to be misstated.



The remuneration policy is available on Danfoss' website. The company believes that the policy complies with the recommendation.

| RECOMMENDATION | | THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON: |
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| <p>4.1.3. The Committee recommends that remuneration of members of the Board of Directors does not include share options.</p> |  | <p>Danfoss no longer uses share option programs in its remuneration of Executive Committee members, other executives or of Board members. Until 2009, however, Danfoss did use share option programs to remunerate Executive Committee members, other executives or Board members.</p> |
| <p>4.1.4. The Committee recommends that if share-based remuneration is provided, such programs be established as roll-over programs, i.e. the options are granted periodically and should have a maturity of at least three years from the date of allocation.</p> |  | <p>Until 2009, Danfoss used roll-over, share-based remuneration for members of the Executive Committee and other executives. The Board has not participated in the program since 2007.</p> |
| <p>4.1.5. The Committee recommends that agreements on termination payments should not amount to more than two years' annual remuneration.</p> |  | |
| <p>4.2. Disclosure of the remuneration policy</p> | | |
| <p>4.2.1. The Committee recommends that the company's remuneration policy and compliance with this policy be explained and justified in the chairman's statement at the company's general meeting.</p> |  | <p>Danfoss does not comply with the recommendation The remuneration policy was reviewed and explained when it was submitted for approval at the annual general meeting.</p> |
| <p>4.2.2. The Committee recommends that the proposed for remuneration for the Board of Directors for the current financial year be approved by the shareholders at the annual general meeting.</p> |  | <p>The shareholders approve the remuneration of the Board for the current accounting year.</p> |
| <p>4.2.3. The Committee recommends that the total remuneration granted to each member of the Board of Directors and the executive Board by the company and other companies in the group, including information on the most important contents of retention and retirement/resignation schemes, be disclosed in the annual report and that the linkage with the remuneration policy be explained.</p> |  | <p>Danfoss has chosen to provide a summary of the remuneration for the Board and the Executive Committee and of other significant benefits. For discretionary reasons, the company does not disclose individual salary conditions.</p> |

| RECOMMENDATION | THE COMPANY COMPLIES IN PART/DOES NOT COMPLY DUE TO THE FOLLOWING REASON: | |
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| 5 Financial reporting, risk management and audit 5.1. Identification of risk and transparency about other relevant information | | |
| 5.1.1. The Committee recommends that the Board of Directors in the management commentary review and account for the most important strategic and business-related risks, risks in connection with the financial reporting as well as for the company's risk management. |  | For information about risk management at Danfoss, see the annual report. |
| 5.2. Whistleblowing | | |
| 5.2.1. The Committee recommends that the Board of Directors decide whether to establish a whistleblower scheme for expedient and confidential notification of possible or suspected wrongdoing. |  | Danfoss has set up an ethical hotline, which employees can use to report any violations of Danfoss' ethics code. In order to ensure a high degree of discretion and confidentiality, Danfoss cooperates on the Hotline with an external company LRN. Reports of any violation of the ethics code will be submitted to Danfoss' Ethics Committee. The committee consists of General Counsel Anders Stahlschmidt and Corporate Ethics & Compliance Officer Ken B. Graversen. |
| 5.3. Contact to auditor | | |
| 5.3.1. The Committee recommends that the Board of Directors ensures regular dialogue and exchange of information between the auditor and the Board of Directors, including that the Board of Directors and the audit committee meet with the auditor at least once a year meet with the auditor without the executive Board present. This also applies to the internal auditor, if any. |  | The Board is in regular contact with Danfoss' external auditors. In addition, the auditors attend audit committee meetings as and when required as well as the Board meeting, at which the Annual Report is discussed and approved. The auditors also submit ongoing reports to the Board via long- form audit reports. Danfoss has set up an internal audit function. This function submits quarterly reports to the Board of Directors and to the company's external auditors. |
| 5.3.2. The Committee recommends that the audit agreement and auditors' fee be agreed between the Board of Directors and the auditor on the basis of a recommendation from the audit committee. |  | On the basis of a recommendation from the audit committee (which is the entire Board), an audit agreement is concluded between the Board and the auditors about the auditors' work and the remuneration for their work. |

ENGINEERING
TOMORROW

