



*The general meeting of HUCNO (Croatian Association of certified Supervisory board members) held on September 26, 2008 adopted the following*

*RECOMMENDATIONS ON REMUNERATION  
OF MANAGEMENT BOARD MEMBERS AND  
EXECUTIVE DIRECTORS  
IN JOINT-STOCK COMPANIES*

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*Zagreb, September 2008.*

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## 1. OBJECTIVE AND PURPOSE OF RECOMMENDATIONS

- 1.1. The Recommendations stipulate the relations between the company and Management Board, that is, the company and executive directors in more detail pursuant to framework specified by the law, and in accordance with recommended practice in this domain.
- 1.2. The Recommendations are of optional nature, they are based on present legislation and Croatian Corporate Governance Codex adopted by Zagreb Stock Exchange and Croatian Financial Services Supervisory Agency (HANFA), and in accordance with European Commission Recommendation on directors' remuneration (2004/913/EC).
- 1.3. The Recommendations are intended for joint-stock companies, and especially for listed companies whose securities are admitted to trading on a regulated market.
- 1.4. The Recommendations stipulate:
  - procedures of encouraging Board members and executive directors for the purposes of achieving higher company's performance;
  - determining provisions of the contract which is concluded between Management Board or executive directors and the company;
  - determining corresponding mechanisms for assigning rights to Board members, that is, executive directors pursuant to determined company's performance and single performance of Board members, that is, executive directors;
  - corresponding relation of rights of Board members, that is, executive directors in relation to complexity of tasks, and their special responsibilities pursuant to existing legislation;

- procedures and allowances related to termination of function of a Board member or executive director.

1.5. The general meeting should be notified by the Supervisory board, that is, Board of directors on fulfilling the Recommendations.

## 2. DEFINITION OF TERMS IN THE RECOMMENDATIONS

- 2.1. “The Codex” is the Corporate Governance Codex adopted by Zagreb Stock Exchange and Croatian Financial Services Supervisory Agency (HANFA).
- 2.2. “Board Member” is a natural person who has been appointed to office of Board member or president of Management Board of a joint-stock company organized according to dualistic governance system of company’s organs.
- 2.3. “Executive director” is a natural person who has been appointed as executive director by the Board of directors of joint-stock company with monistic governance system of company’s organs.
- 2.4. “The company” is a joint-stock company which has been organized in accordance with the Company Act, and in which a Board member, that is, executive director, performs his or her duty.
- 2.5. “Total remuneration”, that is, remunerations based on salaries, represent all earnings in money or benefits in kind, salary paid to the Board member, that is, executive director by the company. Remunerations based on salaries, supports, rewards and others (costs reimbursement and participation in profits, asset receipts in non-monetary form, such as shares, derivative financial instruments, options, and bonuses), salary paid to the Board member, that is, executive director by a third person instead of employer, insurance premiums, all other remunerations paid to the Board member, that is, executive director by the employer based on work contract or some other act, specifying all remunerations of the Board members, that is, executive director.
- 2.6. “Fixed remuneration” is income whose level has been contractually stipulated, and it belongs to Board member and executive director for

the purposes of fulfilling his or her obligations and assuming responsibility.

- 2.7. “Variable remuneration” is remuneration whose level depends on achievement of a certain degree of performance, that is, depends on company performance.
- 2.8. Remuneration in shares, share options, derivative financial instruments, that is, remuneration based on participation in profits, signifies remuneration achieved by assignment or optional purchase of shares, where the value is defined as a level of market value or difference between market value of assigned shares and remuneration, if shares acquisition is based on partial remuneration. Earning based on the capital is determined only if company shares at the time of assignment are rated at the stock market or public markets in accordance with special act.
- 2.9. “Bonus” is every other privilege which belongs to a Board member, that is, executive director, which does not represent monetary earnings. Bonus, for instance, includes discounts, usage of company’s resources for special purposes, and other privileges.
- 2.10. “The capital” indicates company’s stock capital which is specified in accordance with the Company Act and the Accounting Act.
- 2.11. The term “should”/“it is recommended” etc. in the Recommendations has the meaning of good practice.

### 3. PRINCIPLES FOR REMUNERATION OF BOARD MEMBERS AND EXECUTIVE DIRECTORS

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#### *General provisions*

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- 3.1. While determining principles for remuneration of Board members and executive directors, the Supervisory board or the Board of directors should take into consideration the level of company's stock capital and company's asset value, company's ability for achieving revenue and profit, and the overall company's business costs which include entire and joint costs of remuneration of all member of the company, executive directors, and other managers, as well as every member of Supervisory board, that is, Board of directors. The Supervisory board has to take into consideration that overall amounts of remuneration are in appropriate relation to work performed by the Board member, that is executive director, and company's status.
- 3.2. For the needs of these Recommendations, the term "company" implies subsidiaries and dominant company if a Board member, that is, executive director, performs duty of a Board member, that is, executive director in the dominant company.

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#### *Commission for remuneration*

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- 3.3. The Supervisory board, that is, Board of directors should form a special commission for remuneration. The Commission should have at least three members. However, if there is more, the number should be odd.
- 3.4. There will be a majority of independent members of the whole Commission. The Commission for remuneration has to be nominated by a majority of independent members of Supervisory board or non-

executive members of the Board of directors, as well as persons outside the company's organs. Chairman of the Commission for remuneration should be nominated by the Commission members among themselves, and it should be independent, expert person outside the company's organs.

3.5. The Supervisory board, that is, Board of directors undertakes to prescribe the mandate and authority of the Commission which shall:

- propose to the Supervisory board, that is, Board of directors the policy of remuneration of Board members, that is, executive directors which has to refer to all forms of remuneration, and especially to fixed part of remuneration, variable part of remuneration which is related to business performance, pension plan, and severance pays. When it comes to variable part of remuneration which is related to business performance, the proposal has to include recommendations for determining objective criteria of performance assessment,
- propose to the Supervisory board, that is, Board of directors remuneration for certain Board members or executive directors in accordance with company's remuneration policy and assessment of particular director's activity,
- propose to the Supervisory board, that is, Board of directors the appropriate form and content of the contract with Board members,
- monitor amount and structure of remuneration to higher management personnel and give general recommendations to the Management Board in this connection,
- with regard to incentive part of remuneration to the Management Board, that is, executive directors, when this includes share options or other engagements based on share acquisition, consider the general policy of these type of remuneration, and propose to the Supervisory board adequate solutions, as well as examine data which are issued on this subject in the annual report before publishing.

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### *Structure of remuneration*

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3.6. The Board members, that is, executive directors should be paid in proportion to their work, and this remuneration is stipulated by company's Supervisory board, that is, Board of directors.

Remuneration of Board members, that is, executive directors should:

- adequately reflect time, effort, and experience related to their functions,
- ensure adequate incentive which would balance interests of Board members, that is, executive directors with company's interests,
- be specified in a manner which does not endanger ability of Board members, that is, executive directors to bring decisions in the best interest of the company.

3.7. The Board member, that is, executive director, under the conditions specified in the Recommendations, has a right to the following remuneration:

- fixed remuneration for performing duty and tasks, usage of time and loyalty to the company, which is unchangeable and does not depend on business results;
- variable remuneration which is conditioned by business results in a specific business year for:
  - o realization of annual business goals,
  - o for exceeding annual business goals,
- remuneration for a long-term performance, based on measures which determine company's long-term growth and share value growth,
- capital value growth considering the increase in share price,



- special remuneration,
- participation in company's profits.

3.8. The Supervisory board, that is, Board of directors should determine with a Board member, that is, executive director the system of remuneration for performing duty, so that in agreement with a Board member or executive director the following is specified:

- type and level of fixed remuneration
- types of variable remuneration and basic criteria for determining their level in a manner that variable remuneration is determined depending on fulfillment of actual criteria which are specified every year with the annex to the contract between Board members, that is, executive directors and the company
- every year in the annex to the contract between the company and Board members, that is, executive directors, the following is specified:
  - actual goals for the business year which are in accordance with company's strategy and confirmed annual business plan of the company, so that objective criteria for determining their realization are ensured;
  - determining minimum criteria for realization of goals necessary for achieving right to variable part of remuneration.

3.9. The Supervisory board, that is, Board of directors should specify every year actual goals for every business year in accordance with company's strategy and confirmed annual company's plan, so that reliable measuring of their realization is ensured.

3.10. The Supervisory board, that is, Board of directors should bring a decision which sets criteria for determining performance of Board member or executive director, and pursuant to them conclude annex to the contract with a Board member, that is, executive director every year.

3.11. When part of remuneration in form of shares is specified for a Board member, that is, executive director, the share value should be determined in accordance with market price or the fair price if the company's securities are not admitted to trading on a regulated market.

3.12. The methods for specifying level and appropriateness of remuneration should respect elements such as:

- scope of authority of a particular Board member, that is, executive director;
- personal performance in performing business activities;
- size and company's financial status;
- economic environment in which the company operates, especially if the company represents natural monopoly;
- company's performance in relation to other companies with the same business activities;
- fulfillment of strategic and annual plans;
- remuneration of Board members in subsidiaries.

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### ***Fixed remuneration***

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3.13. Fixed remuneration is unchangeable and does not depend on business results.

3.14. Fixed remuneration should include fixed cash inflows and bonuses.

3.15. Fixed remuneration should be determined according to scope of responsibility of a specific Board member, that is, executive director, degree of responsibility, and company's loyalty. Fulfillment of goals determined by annual financial report does not have effect upon specifying fixed remuneration.

- 3.16. The Supervisory board, that is, Board of directors should not specify annual fixed remuneration of Board member, that is, executive director in terms of formula, but in gross monthly amount.
- 3.17. While determining annual fixed remuneration of Board member, that is, executive director, the Supervisory board, that is, Board of directors should take into account the balance of fixed remuneration depending on corresponding remuneration of Board members and executive directors in similar companies, and depending on the importance of a Board member or executive director (knowledge, experience, use of potential, business competence etc.). In the process of determining company's eligibility, criteria of size, activity, and business complexity should be respected.
- 3.18. The annual fixed remuneration level for Board members or executive directors should amount to 85% of annual fixed remuneration level for the Management Board president or chief executive director in the same company.
- 3.19. The relation between annual remuneration levels should be specified depending on competence and, in this connection, increased responsibility of the Management Board president, that is, chief executive director, that is, depending on competence and responsibility of a Board member, that is, executive director.
- 3.20. In general, fixed remuneration should be in the form of fixed cash salaries or in the form of bonuses if by this better motivational effect and company's loyalty is achieved, and if this is suitable to the Board member, that is, executive director.
- 3.21. Fixed bonuses should not exceed 10% of overall fixed remuneration.
- 3.22. The Board member or executive director should be provided with the following as fixed bonuses:
- life insurance and accident insurance,
  - additional health insurance,

- business car of higher class, for business and personal usage,
  - managerial medical check-up once a year, and with emphasis on health condition of the Board member or executive director possibly two times a year.
- 3.23. If the contract with a Board member or executive director has been concluded as employment contract, fixed remuneration in cash, in addition to all bonuses, shall represent the basic salary.

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### *Variable remuneration*

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- 3.24. Variable remuneration is conditioned by business results in a specific business period.
- 3.25. Variable remuneration should be based on company's business performance and business performance of each Board member or executive director.
- 3.26. Variable remuneration should be specified in such a scope that it motivates the Board member or executive director to achieve higher performance level.
- 3.27. Variable remuneration should include variable remuneration for a short-term performance and variable remuneration for a long-term performance.
- 3.28. Variable remuneration should be paid in the form of cash and non-cash inflows. Non-cash inflows should be paid in the form of shares and share options, as well as similar instruments which have the effect of long-term incentives.
- 3.29. Variable remuneration for a long-term performance should be paid in the form of non-cash inflows.

- 3.30. Variable remuneration should be specified and paid once a year for the past business year in the process of adoption of the annual financial report, unless it does not result differently from the nature of variable form of remuneration.
- 3.31. The goals pursuant to which the Supervisory board, that is, Board of directors shall form criteria for measuring performance should be clearly determined in company's annual business plan.
- 3.32. The Supervisory board, that is, Board of directors should monitor fulfillment of goals from company's business plan and indicators' movement once a year.
- 3.33. The goals from the annual business plan, performance indicators, and other elements which have effect upon variable remuneration should be stated in the annual annex to the contract of a Board member, that is, executive director with the company. The annex should be legal basis for payment of variable remuneration.
- 3.34. The Supervisory board, that is, Board of directors should confirm the annual business plan which should be prepared ambitiously and realistically, with regard to performance indicators in the past business year, business performance of similar companies, and in relation to other factors, for which it is expected to have significant effect upon company's business activities, and with regard to company's long-term business plan.

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*Remuneration for a short-term performance*

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- 3.35. Remuneration system with variable remuneration for a short-term performance should be formed in a manner that a Board member, that is, executive director, for achieving goals determined by annual business plan, receives variable remuneration in the amount of approximately 50% of annual fixed remuneration. In case of achieving planned

performance, remuneration in the amount which has not been previously specified could be paid to the Board member, that is, executive director.

3.36. Variable remuneration for realizing annual business plan, which are accounted for a Board member, that is, executive director, should be paid in the form of cash inflows up to the amount of one half, and the remaining part in the form of shares and similar instruments which have an effect of long-term incentives.

3.37. A short-term business performance of a Board member, that is, executive director should be evaluated by way of qualitative and quantitative performance criteria.

3.38. As qualitative criteria, the following indicators should be used:

- financial results
- investments (research and development, innovation acceptance, employee education etc.);
- business procedures (risk management, leadership, quality of work and productivity, public relations, investor relations, etc.);
- non-financial results (employee satisfaction, satisfaction and constancy of clients, company's reputation);
- assessments (social responsibility, ethics, ecology, etc.).

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### *Remuneration for a long-term performance*

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3.39. Remuneration for a long-term performance should include efficient and balanced activity of company's Board member, that is, executive director for achieving company's growth which has been planned for a long-term period.

- 3.40. Remuneration for a long-term performance should not be limited; however, within the instruments pursuant to which a Board member, that is, executive director gains the right to such remuneration, appropriate elements which prevent share value movement manipulation should be incorporated.
- 3.41. It should be made impossible for a Board member, that is, executive director, who has acquired shares pursuant to share options or pursuant to share plan, to alienate share acquired in such manner at least for three years upon termination of term of office in which he or she acquired them. In the new term of office he or she may alienate them only if in the new term of office he or she acquires new shares before alienation of those from the previous term of office.
- 3.42. Compensation and cash payments for unused options should not be allowed.
- 3.43. The Board member, that is, executive director of a subsidiary can accept the shares of dominant company instead of shares of a subsidiary.

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*Special remuneration and participation in company's profits*

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- 3.44. If the company does not have a confirmed plan of remunerating Board members and executive directors for a long-term company's performance in the form of share, option or similar plan, and the Supervisory board and Management Board, that is Board of directors and executive directors justifiably believe that all or certain Board members, that is, all or certain executive directors, pursuant to present remuneration system are not or shall not be sufficiently remunerated for achieved results, they can propose to the general meeting to bring the decision on participation in profits or other special remuneration for Board members, that is, executive directors.

- 3.45. The general meeting should vote on the proposal of decision of the general meeting on the use of profit, which specifies participation in profits or remuneration to the Management Board, that is, executive directors, after they have been provided with correct and complete representation of company's business results, business plan, and all remuneration and compensation of each Board member, that is, executive director, which have been determined based on the contract with the company.
- 3.46. The decision on usage of profit should include elements based on which it shall be possible to decide which share of the profit relates to each Board member, that is, executive director.
- 3.47. In case of decision on participation in profits in this section, the payment of participation in profits should be specified as 50% in the form of cash inflows and as 50% in shares, in which process, the general meeting should know the share price in terms of which they shall calculate the number of corresponding shares to a Board member, that is, executive director.

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### *Costs reimbursement*

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- 3.48. The Board member, that is, executive director, should be provided with costs reimbursement and appropriate remuneration, which appertains also to every employee in the company.
- 3.49. The type of remuneration and costs reimbursement, as well as their level and manner of determining the level, should be specified in the contract with a Board member, that is, executive director.
- 3.50. The Board member, that is, executive director, should have a right to other remuneration pursuant to the Labor Act and collective agreements which are valid for the employees such as: service bonuses,



bonuses for special working conditions, overtime work payment, and other bonuses, holiday cash grant, etc.

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*Liability insurance*

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3.51. The company should stipulate liability insurance in connection with performing duties of company's Board members and executive directors, in a manner to ensure company's interests, especially in terms of company's risk management.

## 4. TRANSPARENCY OF REMUNERATION OF COMPANY'S BOARD MEMBERS AND EXECUTIVE DIRECTORS

- 4.1. The statement on policy of remuneration of Management Board and executive directors should be permanently available by way of Internet on web site of the company on the Internet and can be a part of the annual report.
- 4.2. The statement on policy of remuneration should primarily include company's policy with regard to remuneration of Board members and executive directors for the following business year, and if it is appropriate, for the following years, as well as the overview of how the policy of remuneration of Board members, that is, executive directors has been applied in the previous year. It is especially important to emphasize significant modification in relation to remuneration policy compared to the previous year.
- 4.3. The statement on policy of remuneration should include the following parts:
- explanation of relative share and importance of fixed and variable remuneration components,
  - sufficient information on criteria of performance upon which fulfillment the right to acquisition of share options, shares or other form of variable part of remuneration is based,
  - sufficient information on connection between remuneration level and performance,
  - principal indicators and reasons for assignment of annual bonuses or privileges of non-cash nature,

- summary of contract with Board members which has to include data on contract's validity, termination period, and especially severance pays. Every form of remuneration of Board members, that is, executive directors, which includes share options or other rights for share acquisition, or if remuneration is based on company's share price, should be approved by company's general meeting before coming into effect. This approval refers to remuneration principles and not on approval of remuneration to certain Board members or executive directors.
- 4.4. Information on the policy of remuneration of Board members, that is, executive directors, should be available to the shareholders, as well as all information on former policy of remuneration of Board members and executive directors, if the same has been modified in the period of last two years.
  - 4.5. The policy of remuneration of Board members, that is, executive directors should be announced in advance in the report of Supervisory board, that is, Board of directors to the general meeting.
  - 4.6. Information on remuneration of Board members, that is, executive directors should be available to the shareholders, including options and other privileges.
  - 4.7. Information should be announced to the shareholders in the attachment of company's annual business reports and annual consolidated financial reports, as well as in the report of Supervisory board, that is, Board of directors on company's general meeting.
  - 4.8. The Supervisory board, that is, Board of directors should specify in the decision on nomination and in the contract with a Board member, that is, executive director that his or her remuneration can be publicly announced.
  - 4.9. All types of remunerations of Board members, that is, executive directors should be announced in the annual company's report, so that

the announcement is comprehensible, specified in detail according to level, types, and remuneration.

4.10. While announcing, remuneration should be arranged in groups:

- fixed remuneration;
- variable remuneration;
- remuneration for a short-term performance
- remuneration for a long-term performance

4.11. While announcing variable remuneration, the manner of fulfilling criteria, which is the basis for assigning variable remuneration, should be announced.

4.12. The reports have to be created in a thorough and truthful manner; they need to be created in due time, and usually in writing.

## 5. CONTRACT WITH A BOARD MEMBER, THAT IS, EXECUTIVE DIRECTOR

5.1. The contract with a Board member, that is, executive director should include the following provisions:

- clear definition of type of contract being concluded, and that it is the matter of contract of the company with a Board member, that is, executive director;
- obligation of a Board member, that is, executive director connected with the annual business plans and company's strategy;
- specifying remuneration system, structure, and individual types of remuneration,
- specifying fixed cash inflows and bonuses for performing duty, variable remuneration for achieving performance, and costs reimbursement,
- specifying the level of fixed cash inflows in gross monthly amount;
- specifying manner of determining what is justified and the level of variable cash and non-cash remuneration for a short-term and long-term performance,
- specifying that actual norms, criteria, and manner of determining level of variable remuneration are determined in the annual annex to contract of the company with a Board member, that is, executive director.

5.2. Measurable goals and tasks should be specified in the annual business plan, whose non-fulfillment means non-fulfillment of business plan in its entirety and represents a reason for recall of a Board member, that is, executive director.

5.3. If after specifying total remuneration of a specific Board member, that is, executive director company's circumstances deteriorate so significantly that further payment of remuneration would signify severe injustice, the Supervisory board, that is, Board of directors shall be authorized to reduce it appropriately.

5.4. Reduction of remuneration from the previous paragraph does not have an effect on other parts of the contract of a Board member with the company. The Board member has a right to terminate the contract at the end of following quarter on condition that the termination period for this is six weeks.

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*Recommendations coming into effect*

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The Recommendations shall come into effect as of the day when they are adopted by the Assembly of HUCNO. The Recommendations shall be published on the website [www.hucno.hr](http://www.hucno.hr).