october

2008

RECOMMENDATIONS CONCERNING THE COMPENSATION OF EXECUTIVE DIRECTORS OF COMPANIES WHOSE SHARES ARE ADMITTED TO TRADING ON A REGULATED MARKET

AFEP
Association Française
des Entreprises Privées

MEDEF

RECOMMENDATIONS
CONCERNING THE COMPENSATION OF EXECUTIVE DIRECTORS OF COMPANIES WHOSE SHARES ARE ADMITTED TO TRADING ON A REGULATED MARKET

Introduction

Boards of directors and supervisory boards are responsible for determining the compensation of executive directors, based on proposals made by the compensation committee. If some of these recommendations are not complied with, the board of directors or supervisory board must explain the reasons for such non-compliance, in accordance with the "comply or explain" principle.

In order to determine the said compensation, the relevant boards and committees must take into account the following principles:

- Comprehensiveness: the compensation determined through this process must be complete. Fixed components, variable components (bonus), stock options, performance shares, directors' fees, pension terms and specific benefits must be taken into account when determining the overall compensation level.
- Balance between the compensation components: each compensation component must be clearly substantiated and correspond to the general interest of the company.
- Benchmark: the compensation must be assessed within the context of a business sector and the benchmark European or global market.
- Consistency: the executive director's compensation must be determined in a manner consistent with that of the other officers and employees of the company.
- Clarity of the rules: the rules must be simple, stable and transparent. The performance criteria used in order to determine the variable part of the compensation or where applicable the award of options or performance shares, must correspond to the company's objectives, and be demanding, explainable, and, to the greatest extent possible, long-lasting.
- Reasonableness: the method of determining the compensation and award of stock options and performance shares must be balanced and take into account at the same time the company's general interest, market practices and officer performance.

RECOMMENDATIONS

Scope

These recommendations are intended for companies whose shares are admitted to trading on a regulated market.

It is also advised and recommended that those companies whose shares are admitted to trading on an organized market (Alternext) as well as unlisted companies apply these recommendations, in whole or in part, as is already the case for many corporate governance rules, while adapting them to their company's own specific features.

These recommendations apply to executive directors of the above companies: chairman and chief executive officer, deputy chief executive officers of companies having a board of directors, members of the management board of companies having a management board and a supervisory board, and statutory managers of limited stock partnerships.

Nature of the recommendations

These recommendations primarily consist in general rules that must guide actions taken by the compensation committees. The implementation of these rules is to be defined according to the specific features of each company (size, industry). These recommendations operate together with, supplement and clarify the AFEP / MEDEF corporate governance code.

1. Termination of the employment contract in the event of appointment to a corporate office

This recommendation applies to the chairman, to the chief executive officer of companies having a board of directors, to the chairman of the management board, to the sole managing director of companies having a management board and a supervisory board, and to statutory managers of limited stock partnerships.

This recommendation does not apply to those employees of a group of companies who are officers of a subsidiary of the group.

The high level of compensation of executive directors of listed companies is justified in particular by the assumption of risks. Accordingly, such compensation cannot be granted concurrently with the benefits of an employment contract.

Accordingly, when a senior executive becomes an executive director of the company, it is recommended to terminate his or her employment contract with the company, either contractually or by resigning.

This recommendation applies to appointments made after the publication of this recommendation and to the renewal of any appointment to a corporate office made before such publication, at the discretion of the board of directors or supervisory board.

2. Final elimination of any unfair termination payments (“golden parachutes”)

It is not acceptable that executive directors of companies that have failed or executive directors who have themselves failed may leave their company and receive severance payments.

The law gives a central role to shareholders, imposes total transparency and makes termination payments conditional on performance requirements. The performance requirements imposed by the boards must be demanding and may authorize the indemnification of an executive director only in the event of an imposed departure linked to a change of control or change in strategy.

Termination payments may not be granted to executive directors who decide to leave the company in order to hold another position or change their position within the group or are entitled to exercise their rights to pension in the near future.

Where applicable, the termination payments may not exceed two years of compensation (fixed and variable).

These rules and the above-mentioned cap apply to all indemnities and include in particular any indemnities paid pursuant to a non-compete clause.

Any artificial increase in the compensation during the period preceding the departure is to be prohibited.

3. Strengthening the supervision of the additional pension rights

The companies’ right to offer additional pension schemes to their executive directors must comply with conditions, so as to avoid any abuse.

Additional defined benefit pensions are subject to the condition that the beneficiary is a director or employee of the company when asserting his or her pension rights under the applicable rules.

In order to prevent any abuse, it is necessary to define certain additional rules:

- the value of the relevant benefit must be taken into account when determining the overall level of the compensation on the basis of the general principles stated at the beginning of this document.
- the group of potential beneficiaries must be significantly broader than the group of executive directors.
- the beneficiaries must meet reasonable seniority levels (i.e. time spent) within the company, as determined by the board of directors or the management board.
- the potential annual benefits may only represent a limited part of the beneficiary's fixed compensation.
- the benchmark period used to calculate the benefits must last several years, and it is necessary to avoid any artificial increase in the compensation over the said period for the sole purpose of increasing the pension scheme's return.

Therefore, it is necessary to exclude any schemes that give a right, whether immediately or over few years, to a high percentage of the total compensation at the end of the career.

4. Determination of additional rules relating to stock options and the award of performance shares

- Save for certain specific structures (such as start-up companies), the award of stock options must reflect a policy aimed at having the beneficiaries participate in the capital, i.e. at aligning the beneficiaries' interests, with an assumption of the relevant risks, and not achieving instantaneous additional compensation. The options' exercise terms should be adapted accordingly.

- If the award of stock options does not extend to all employees, it is necessary to provide for another mechanism involving the employees in the company's performance (incentive, exceptional profit-sharing agreement, award of bonus shares, etc.).

- The award of performance shares to executive directors must be conditional on performance requirements. Any award of bonus shares not subject to any performance requirements must be reserved for employees, in accordance with their purpose, i.e. to develop employee share ownership, as provided for by law which created the relevant scheme.

- Award

  - It is necessary to ensure that the stock options and performance shares valued in accordance with the IFRS standards do not represent a disproportionate percentage of aggregate compensations, options and shares awarded to each executive director. To that end, the boards must assess the award of new options and shares having regard to all the components of compensation of the relevant executive director. The board shall be responsible for determining the maximum percentage of the relevant compensation (in accordance with market standards) that such awards should not exceed.
  - Companies must avoid awarding an excessive proportion of their bonus shares and options plans to executive directors. The boards shall be responsible for defining, according to the circumstances of each company (size of the company, industry, scope of responsibilities, number of officers, etc.), the maximum percentage of stock options and performance shares that may be awarded to executive directors, as compared with the aggregate amount approved by the shareholders.
  - The awards must be made in the same calendar periods, for example, after publication of the financial statements for the previous financial year, and if suitable each year, in order to limit any windfall effect.
  - It is necessary to prohibit any windfall effects related to a “bear” market. The number of awarded stock options and performance shares may not deviate from earlier corporate practices, save in the event of a material change made to the scope of the business, warranting a change in the applicable scheme.
  - According to the terms set by the board and made public upon the award, vesting of any performance shares awarded to executive directors must be conditional on the acquisition of a defined quantity of shares at the time when the beneficiary has the disposal of the awarded shares.

- Prices

  - It is necessary to ban any discount on the exercise price for all beneficiaries.
  - It is necessary to prohibit any option hedging instruments.

- Exercise

  - It is necessary to ensure that the exercise by executive directors of all stock options and the acquisition of their bonus shares are linked to performance requirements that must be satisfied over a period of several consecutive years. These conditions must be serious and demanding, and must combine internal performance requirements to the company and external performance requirements, such as requirements linked to the performance of other companies or an industry benchmark.

- It is necessary to determine the periods preceding the publication of the financial statements, during which the stock options may not be exercised. The board of directors or supervisory board must determine the said periods and where applicable determine the procedure to be followed by executive directors before exercising any stock options, in order to ensure that they do not hold any information likely to prevent such exercise.

▪ Obligation to hold the acquired shares

The executive directors must be obliged to keep a material number, increasing over time, of the securities acquired.

The board may choose either a reference to annual compensation to be determined for each executive director and/or a percentage of the net capital gain, after the sales necessary for the exercise of the stock options and the payment of the taxes, social security contributions and expenses necessary for the transaction, or a fixed number of shares.

Regardless of the reference used, the number of shares to be held must be compatible with the applicable performance criteria and must be periodically revised in light of the director's situation, at least upon each renewal of the corporate office.

5. Improve the transparency of all compensation items

The components of compensation applicable to each executive director must be made public on an individual basis, in accordance with applicable provisions of law and the further recommendations issued by AFEP and MEDEF. However, the clarity of the said information can still be improved.

To that end, it is recommended to:

- comply with the standardized format defined by AFEP and MEDEF (see attached tables) as regards all director compensation components (including the valuation of the awarded stock options based on the method selected for the consolidated financial statements);
- disclose all components of the executive director compensation, whether potential or vested, immediately after the meeting of the board approving the same.

6. Monitoring of the recommendations

In each company's annual management report (document controlled by the French Financial Market's Authority), it is necessary to state, in accordance with the Act of 3 July 2008, whether the company enforces the AFEP-MEDEF corporate governance code, as supplemented and clarified by these recommendations. Otherwise, the companies must explain in the same public document the reasons why they have not applied these recommendations.

In order to ensure the actual application of the "comply or explain" corporate governance rule, AFEP and MEDEF analyze the information disclosed by the relevant companies. If AFEP and MEDEF note that any company does not apply any of these recommendations and do not provide sufficient explanations, they will contact the corporate executive officers concerned.

Furthermore, an aggregate report on the developments in the monitoring of these recommendations shall be made public each year.

SCHEDULE

STANDARDISED FORMAT FOR THE DISCLOSURE OF THE COMPENSATION OF EXECUTIVE DIRECTORS OF COMPANIES WHOSE SECURITIES ARE ADMITTED TO TRADING ON A REGULATED MARKET

In order to improve the clarity and comparability of the information concerning the compensation of executive directors, AFEP and MEDEF recommend the following format to those companies whose shares are admitted to trading on a regulated market.

These seven tables must be grouped in a specific section of the reference document dedicated to the compensation of executive directors. These tables supplement, but do not replace, the information that must be otherwise furnished by the above-mentioned companies, for instance as regards their compensation policy, the criteria for determining the variable component of remuneration or full features of past stock option plans.

Furthermore, these tables must be read in conjunction with the information necessary to fully understand them and by any information that may not be included in tables, such as for instance the features of collective benefit schemes and pension schemes entailing a risk factor.

Table 1

Summary table of the compensation, options and shares accruing to each executive director		
Name and position of the executive director	Financial year N-1	Financial year N
Compensation due in respect of the financial year *(detailed in table 2)*		
Valuation of the stock options awarded during the financial year *(detailed in table 4)*		
Valuation of the performance shares awarded during the financial year *(detailed in table 6)*		
TOTAL		

Table 2

Summary table of the compensation of each executive director				
Name and position of the executive director	Amounts for financial year N-1		Amounts for financial year N	
	due	paid	due	paid
- fixed compensation				
- variable compensation				
- extraordinary compensation				
- directors' fees				
- fringe benefits[1]				
TOTAL				

Table 3

Non executive Directors' fees table		
Board members[2]	Directors' fees paid in year N-1	Directors' fees paid in year N
TOTAL		

[1] These fringe benefits must be described: car, housing, etc.
[2] It is necessary to include in this column all members of the board of directors, even where the said information is already included in the tables concerning the individual compensation of executive directors.

Table 4

Share options awarded during the financial year to each executive director						
Options awarded to each executive director by the issuer and by any company of the group (nominative list)	Number and date of the plan	Nature of the options (purchase or subscription)	Valuation of the options according to the method used for the consolidated financial statements	Number of options awarded during the financial year	Exercise price	Exercise period

Table 5

Stock options exercised during the financial year by each executive director				
Options exercised by executive directors (nominative list)	Number and date of the plan	Number of options exercised during the financial year	Exercise price	Award year

Table 6

Performance shares awarded during the financial year to each executive director					
Performance shares awarded during the financial year to each executive director by the issuer and by any company of the group (nominative list)	Number and date of the plan	Number of shares awarded during the financial year	Valuation of the shares according to the method used for the consolidated financial statements	Acquisition date	Availability date

Table 7

Performance shares that have become available during the financial year for each executive director				
Performance shares awarded during the financial year that have become available for each executive director (nominative list)	Number and date of the plan	Number of shares that have become available during the financial year	Acquisition terms	Award year