

**REPORT PREPARED BY THE APPOINTMENTS AND REMUNERATION COMMITTEE OF EUSKALTEL, S.A. IN RELATION TO THE PROPOSED RESOLUTION REGARDING THE COMPANY'S DIRECTOR REMUNERATION POLICY REFERRED TO IN ITEM TEN ON THE AGENDA FOR THE ANNUAL GENERAL MEETING OF SHAREHOLDERS OF THE COMPANY CALLED FOR 1 APRIL 2019, ON FIRST CALL, AND FOR 2 APRIL 2019, ON SECOND CALL**

**I. Introduction**

Pursuant to the provisions of section 529 *novodecies* of Royal Legislative Decree 1/2010, of 2 July, approving the restated text of the Corporate Enterprises Act (the “**Corporate Enterprises Act**”), the Appointments and Remuneration Committee of Euskaltel, S.A. (“**Euskaltel**” or the “**Company**”), at its meeting of 27 February 2019, formulates and approves this report on the proposed director remuneration policy for this financial year 2019 and financial years 2020 and 2021 (the “**Remuneration Policy**”), which the Company’s Board of Directors will submit for approval at Euskaltel’s General Meeting of Shareholders scheduled for 1 and 2 April 2019, on first and second call, respectively (the “**Report**”).

**II. Director remuneration policy**

**1. Effective term**

The Remuneration Policy shall apply during this financial year 2019 and the next two financial years (2020 and 2021), unless the shareholders acting at a General Meeting of Shareholders of Euskaltel resolves to amend or replace it during such period, all in accordance with the provisions of section 529 *novodecies* of the Corporate Enterprises Act.

**2. Principles and rationale**

Pursuant to article 27 of the Regulations of the Board of Directors of the Company, and within the limits set out in the Company’s Bylaws, the Board of Directors shall endeavour to ensure that the remuneration of the directors is reasonably commensurate with the prominence of the Company, the financial situation thereof at any particular time and the market standards used at companies of a similar size or activity, and takes into account their dedication to the Company. The remuneration system established should be focused on promoting the long-term profitability and sustainability of the Company and include the safeguards required to avoid the excessive assumption of risk or rewarding unfavourable results.

The Board of Directors shall also ensure that the amount of the remuneration of external directors is such that it provides incentives to their dedication but does not compromise their independence.

In line with the foregoing, the Remuneration Policy is based on the following principles:

- **Moderation:** remuneration should be reasonably proportional to the Company, the economic situation thereof at any particular time and market standards for comparable companies.
- **Suitability:** the Remuneration Policy shall be focused on the attraction, motivation and retention of valuable human capital, as well as on remunerating professional merit, responsibility assumed and dedication in the case of external non-executive directors.
- **Balance:** the Remuneration Policy shall establish a suitable balance between fixed and variable components, such that fixed remuneration is a sufficiently high percentage of

total remuneration that it allows the introduction of measures of flexibility for directors who perform executive duties.

- Profitability and sustainability: the remuneration of directors performing executive duties shall incentivise performance and shall reward the creation of long-term value.
- Link to results: the remuneration of directors who perform executive duties shall include the required link to the Company's results over an appropriate time period, aligning with the interests, values and strategy of the Company.
- Fairness and external competitiveness: the external competitive environment and the principles of internal fairness shall be taken into account when establishing director remuneration.
- Transparency of the remuneration policy: the Remuneration Policy shall be established, determined and applied in accordance with applicable law, the internal rules of the Company and best corporate practices, ensuring transparency and adherence to the Good Governance Code of listed companies approved by the National Securities Market Commission on 18 February 2015 (the "**Good Governance Code**"). In particular, the Company shall make available to the shareholders on occasion of the call to the Annual General Meeting the Annual Director Remuneration Report, which shall be submitted to a consultative vote as a separate item on the agenda.

The Remuneration Policy essentially differentiates between those directors who are not entrusted with executive duties from those others who are entrusted with executive duties at the Company, as described below.

### **3. Maximum amount of annual remuneration to be paid to the directors as a whole**

Pursuant to the Company's Bylaws, the shareholders acting at a General Meeting of Shareholders must determine the maximum remuneration to be received by the directors for all of the duties that they perform, both executive and non-executive.

Pursuant to the foregoing and the principles governing this Remuneration Policy, the maximum amount of annual remuneration for all directors that proposed to the Board of Directors so that it in turn so proposes to the shareholders at the General Meeting of Shareholders, is established at 4,500,000 euros.

This maximum amount shall remain in effect for so long as a change thereof is not approved by the shareholders acting at a General Meeting.

For purposes of clarification, it is stated for the record that such amount does not entail an increase in the remuneration of the directors under any circumstances.

The purpose of the shareholders determining the maximum remuneration to be received by the directors for all of the duties they perform, both executive and non-executive, is only to avoid the occurrence of a potential tax risk consisting of the inability to deduct as an expense the amounts to be paid to the members of the Board of Directors.

### **4. Remuneration of directors who are not entrusted with executive duties**

The remuneration of directors who are not entrusted with executive duties is made up of a fixed allocation that is paid entirely in cash and remunerates membership on the Board of Directors and on any of its various Committees, without distinguishing duties or positions

held, unless the Board of Directors otherwise provides, including any particular provision on remuneration, for the lead independent director.

Along these lines, the Board of Directors may make additional allocations to the lead independent director for the performance of duties inherent to such position. The amount of such additional allocation, if any, shall be determined by the Board of Directors on an annual basis, and may not, considered individually, exceed 25% of the annual fixed remuneration corresponding to the director for membership on the Board of Directors.

The Board of Directors has approved the following amounts:

- Annual fixed allotment for membership on the Board of Directors in accordance with market standards. The fixed allotment for this item is 65,000 euros for financial year 2019.
- Annual fixed allotment for membership on each advisory Committee of the Board of Directors, determined with market standards. The fixed allotment for this item is 15,000 euros for financial year 2019.
- Cash remuneration consisting of the payment by Euskaltel of insurance premiums, which must be approved by the Board of Directors. The annual maximum limit for 2019 is established at 8,000 euros for each director.
- A civil liability policy upon customary terms and proportional to the circumstances of the Company. The maximum amount of this coverage for 2019 is 10,000,000 euros.

For purposes of clarification, it should be noted that the foregoing items of remuneration are received only by directors who are not entrusted with executive duties, as the executive directors will only receive the remuneration established in their respective contracts, as described in section 5 below.

## **5. Remuneration of directors for the performance of executive duties**

The remuneration system for executive directors is therefore made up of:

- Annual fixed remuneration.
- Annual variable remuneration calculated based on benchmark qualitative or quantitative indicators or parameters linked to the level of achievement of their objectives (approved by the Board of Directors, upon a proposal of the Appointments and Remuneration Committee).
- Long-term variable remuneration based on the delivery of cash or shares, share options or instruments or other remuneration indexed to the value thereof, linked to business objectives, the value of the shares and, if applicable, other corporate social responsibility objectives.

If indexed to shares of the Company or to financial instruments linked to the quoted price thereof, said remuneration must be approved by the shareholders at a General Meeting of Shareholders. If applicable, the resolution shall state the maximum number of shares to deliver, the exercise price or system for calculating the exercise price of the share options, the value of any shares used as a reference, and the duration of the plan.

- The following remuneration: (i) availability of company vehicle; (ii) life and casualty insurance; (iii) special health insurance; and (iv) the ability to enjoy all those benefits that the Company might make available to management personnel.

- A civil liability policy obtained by the Company for its directors upon customary terms and proportional to the circumstances of the Company.
- Potential severance payment for cessation in office or termination of contractual relationship with the Company.

#### *5.1. Annual fixed remuneration*

The fixed remuneration is intended to remunerate the performance of executive duties.

Fixed remuneration (i) shall be mainly based on a market focus and consider the size, nature and scope of the activities of the Company; and (ii) shall be duly aligned with the remuneration at comparable companies in the industry at the domestic and international level.

The fixed remuneration of the Chairman and of the CEO shall be updated annually by the Board of Directors upon a proposal of the Appointments and Remuneration Committee.

The Company shall timely report on the current system and levels of remuneration of the executive directors through the corresponding Annual Director Remuneration Report.

Along these lines, the annual fixed remuneration for financial year 2019 is 347,027.18 euros for the Chairman and 376,498.78 euros for the CEO.

#### *5.2. Annual variable remuneration*

As indicated above, annual variable remuneration only applies to the executive directors as a percentage of their fixed remuneration. Such variable remuneration is based on objective standards that seek to evaluate their contribution to the Company's business objectives in the performance of their executive duties.

Such annual variable remuneration of the executive directors generally ranges between 0% and 75% of the fixed salary at most for the CEO and between 0% and 60% for the Chairman, in both cases accounting for 50% of the fixed salary for achievement of 100% of the goals.

The setting of the objectives, as well as the achievement scales and performance evaluation, are within the purview of the Board of Directors, which will subsequently determine the level of achievement of the business goals used as a reference and the level of achievement of annual variable remuneration (including instances of under-performance and over-performance, as applicable).

Generally, the parameters to be taken into account for determining compliance with the annual variable remuneration objectives, as well as the respective weighting thereof, will be determined annually by the Board of Directors, upon a proposal of the Appointments and Remuneration Committee, based on indicators correlated to Company variables relating to the performance of the business and any other items of a qualitative or quantitative nature including, but not limited to, medium- and long-term sustainability, meeting strategic objectives or objectives relating to corporate social responsibility.

The aforementioned goals and parameters will also take account of the risk assumed to obtain a result and will pursue a balance amongst the Company's short-, medium- and long-term objectives, not revolving solely around one-off, occasional or extraordinary facts or data.

In all cases, executive directors shall be subject to the application of the objectives, parameters and weightings approved by the Board of Directors for the Company's management team generally.

The Board of Directors, upon a proposal of the Appointments and Remuneration Committee, may adjust said weightings or include other objectives that have priority for the short-term development of the business.

The annual variable remuneration system shall be updated regularly by the Appointments and Remuneration Committee, which shall determine whether it is sufficient to measure the contribution to the results of Euskaltel.

By way of example, the parameters for annual variable remuneration applicable to this financial year 2019 and the respective weighting thereof are described below:

- Ebitda – Customers: 40%.
- Cash flow/Revenue: 35%.
- Weighted churn: 15%.
- Corporate Social Responsibility (CSR)/Compliance: 10%.

For each financial year, the objectives and metrics shall represent a proper balance between financial and operational aspects of the Company.

Should the Company's auditors make qualifications in their audit report affecting one or more of the objectives and parameters that are to be taken into account in setting the annual variable remuneration of the executive directors, said qualifications shall be taken into account by the Board of Directors in setting the variable remuneration to be received by the executive directors.

The Company may also demand reimbursement of all or part of the variable remuneration, as applicable, if (i) the payment of the variable remuneration did not match the conditions for performance of the Company; or (ii) the variable remuneration was paid in light of data subsequently proven to be incorrect (e.g. if there was a correction to the annual accounts on which the variable remuneration was based).

### *5.3. Long-term variable remuneration based on the delivery of cash or shares, share options or instruments or other remuneration indexed to the value thereof*

The executive directors may participate in long-term incentive plans linked to strategic conditions and objectives that are payable in cash or in shares established by the Company for its senior officers.

Within the remunerative framework described above, the Board of Directors approved a 2017-2019 Incentive Plan for executive directors and senior officers that allows the beneficiaries to receive in financial year 2020 a certain extraordinary variable cash remuneration with the possibility of total or partial payment in shares in the case of the executive directors, provided that there is compliance with the condition of continuity in office as well as the strategic business objectives and creation of value for the shareholders.

Along these lines, at the General Meeting of Shareholders held on 27 February 2016, the shareholders approved the potential delivery of a maximum of up to 180,000 shares to the executive directors within the framework of the incentive plans, allowing for total or partial payment of the Plan in shares of the Company.

The 2017-2019 Incentive Plan includes best market practices and the recommendations of leading proxy advisors, institutional investors and the Good Governance Code of Listed Companies:

- Establishes clear grant levels for each level of beneficiaries near the average for the market.
- Establishes a 3-year measurement period.
- Establishes an additional holding period for the shares.
- Represents a prudent percentage of capitalisation value.
- Combines financial targets with share price increase targets.
- Paid totally or partially in shares.
- Includes competitive achievement scales.
- Circumscribes variable remuneration in shares for the executive directors.

At the end of the Plan, the Board of Directors intends to approve a similar new Incentive Plan for the 2020-2022 period consistent with the defined remuneration framework, following a favourable report from the Appointments and Remuneration Committee.

#### *5.4. Other remuneration*

The executive directors may receive certain remuneration in kind, including the availability of a company vehicle, a life and casualty insurance policy, a special health insurance policy, and the ability to enjoy all those benefits that the Company might make available to management personnel.

#### *5.5. Benefits*

Except as already stated in sections 4 and 5 of this Report, there are no commitments with respect to pensions, life insurance or otherwise for the directors of the Company.

#### *5.6. Principal terms and conditions of the contracts of the executive directors with the Company*

The contracts that the executive directors sign with the Company are based on the following basic terms and conditions:

##### a) Term:

The contracts of the executive directors shall remain in force for so long as they hold office.

##### b) Severance pay:

The contracts with the executive directors may contemplate severance payment to them in the event of termination.

##### c) Exclusivity and post-contractual non-competition clause:

The contracts may establish an obligation of exclusivity and full dedication to the Company and of post-contractual non-competition for a maximum period of two (2) years from the termination of the contract.

If a post-contractual non-competition clause is established, the contract must provide compensation for this commitment.

## **6. Application of the Remuneration Policy**

Without prejudice to the provisions of the Corporate Enterprises Act regarding director remuneration policies, this Appointments and Remuneration Committee shall endeavour to ensure compliance with the Remuneration Policy and the regular update thereof, and shall propose the amendment and update thereof to the Board of Directors, for submission to the shareholders at a General Meeting, all pursuant to the provisions of the Regulations of the Appointments and Remuneration Committee.

### **III. Conclusions**

Pursuant to the provisions of section 529 *novodecies* of the Corporate Enterprises Act, the Appointments and Remuneration Committee of Euskaltel hereby submits this Report on the Director Remuneration Policy of Euskaltel to the Company's Board of Directors so that it may in turn propose it to the shareholders at the General Meeting of Shareholders for approval, the Appointments and Remuneration Committee having concluded in light of all of the foregoing that the Remuneration Policy:

- (i) Is in accordance with applicable law, and particularly with the Corporate Enterprises Act, as well as with the Good Governance Code and best remuneration practices.
- (ii) Also conforms to the standards of (a) transparency in the information made available to the shareholders; (b) alignment with corporate governance best practices and current standards; and (c) long-term profitability and sustainability of the Company.

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In Derio, on 27 February 2019