Note 8 - Board of Directors' statement on executive management remuneration

Board of Directors' statement on executive management remuneration
The statement on the remuneration of the company’s Chief Executive Officer (CEO) and other members of the Corporate Management Board has been prepared in accordance with the provisions of the Norwegian Public Limited Companies Act, the Norwegian Accounting Act and the Norwegian Code of Practice for Corporate Governance.

Guidelines for executive management remuneration
Hydro’s guidelines for the remuneration of the company’s CEO and other members of the Corporate Management Board reflect Hydro’s global human resources policy, whereby “Hydro shall offer its employees an overall compensation package that is competitive and in line with good industry standards in the country in question. Where appropriate this package should include, in addition to the base salary, also a performance-based incentive that overall shall reflect individual performance.”

Process for determination of remuneration
The Board of Directors has appointed a separate compensation committee consisting of the board chairperson and one shareholder-elected board member, as well as one employee-elected board member. The CEO normally participates in the committee’s meetings unless the committee is considering issues regarding the CEO. Other representatives of senior management may attend meetings if requested to do so.

The committee functions as an advisory body for the Board of Directors and the CEO and is responsible primarily for:

- Making recommendations to the Board of Directors based on the committee’s evaluation of the principles and systems underlying the remuneration of the CEO and other members of the Corporate Management Board.
- Making recommendations to the Board of Directors based on the committee’s evaluation of the overall remuneration of the CEO, including the annual basis for bonus payments and bonus payments actually made.
- Assisting the CEO by consulting on the remuneration of the other members of the Corporate Management Board.
- Advising the Board of Directors and the CEO in remuneration matters which the committee finds to be of material or principal importance for Hydro.

Key principles for determination of remuneration in the coming financial year
The following statement regarding the remuneration of members of the Corporate Management Board will be presented for an indicative vote to the annual general meeting to be held in May 2017. The Board of Directors proposes that the principles set forth below shall apply for 2017 and up until the Annual General Meeting in 2018.

The remuneration of members of the Corporate Management Board shall reflect at all times the responsibility of the CEO and the other members of the Corporate Management Board for the management of Hydro, taking into account the complexity and breadth of the company’s operations, as well as the growth and sustainability of the company. The total remuneration will be rooted in the company’s objective of being competitive, but not a remuneration leader, within the relevant labor markets, while at the same time reflecting Hydro’s international focus and presence.

Hydro attaches importance to transparency and to ensuring that remuneration arrangements are developed and implemented in accordance with principles for good corporate governance.

The total remuneration of the CEO and other members of the Corporate Management Board consists of a fixed compensation, performance-based bonus, share-based long-term incentive plan, employee share plan, pension and insurance arrangements and, in certain cases, a severance pay arrangement. The Board of Directors will continue to ensure moderation in executive management remuneration.

Fixed compensation
The fixed compensation provided to members of the Corporate Management Board includes a base salary (which is the main element of remuneration) and benefits in kind such as a company car or car allowance, a telephone, newspapers and other
similar benefits. The base salaries of individual members of the Corporate Management Board are evaluated annually in light of the complexity and responsibility of the relevant employee’s role and his or her contribution, qualifications and experience, together with conditions in the labor market and general salary trends.

**Variable compensation**

**Bonus**

The maximum annual performance-based bonus payable to the CEO is equal to 50 percent of his or her annual base salary. The maximum annual performance-based bonus payable to the other members of the Corporate Management Board on Norwegian terms of employment is equal to 40 percent of his or her annual base salary. The Board of Directors evaluates and determines annually the bonus system for the CEO and members of the Corporate Management Board. Bonus payments to the CEO and the other members of the Corporate Management Board are dependent on Hydro achieving positive underlying earnings before interest and tax (EBIT). The bonus parameters are established as part of the annual business-planning process with the objective of having parameters that are ambitious and balanced, and objective and measurable, and which reflect the varied nature of Hydro’s operations. The annual bonus shall be determined on the basis of a total assessment of the following elements:

(a) achievement of a pre-defined target for EBIT,

(b) achievement of strategic, operational, financial, and organizational goals, referred to as “key performance indicators” (KPIs). Depending on the business area, these goals can include, among other things,

- productivity and improvements including optimizing of production and margins
- resource allocation and availability
- cost reduction and control
- investment projects
- technology
- quality control
- health, safety, environment, corporate social responsibility, and compliance
- customer relations
- organization development

and possibly other goals derived from the company’s KPI catalog approved by the Board of Directors in 2014,

(c) contribution to the company’s development, as well as compliance with and the promotion of Hydro’s core values (The Hydro Way) and achievement of individual targets, and

(d) the Board of Directors’ overall discretionary assessment.

Bonus payments are not taken into account when determining the basis for pensionable salary.

**Long Term Incentive (LTI)**

The company has a share-based long-term incentive plan for the CEO and the other members of the Corporate Management Board of 30 percent of annual base salary. LTI payments are dependent on Hydro achieving positive underlying earnings before interest and tax (EBIT) for the previous financial year. The terms of this plan are changing in 2017. Payments will henceforth be based partly on achieved return on capital employed, and partly on return on capital employed measured against a weighted average of return on capital employed from comparable companies. Recipients of LTI payments are required to invest the after-tax net amount in Hydro shares with a lock-in period of three years. Any holder of such shares who voluntarily terminates his or her employment during such a three-year period must pay to the company an amount equal to the after-tax value of the relevant shares at or around the last day of employment. The LTI plan is subject to annual evaluation and decision by the Board of Directors. LTI payments are not taken into account when determining the basis for pensionable salary.

The company does not offer options or other similar arrangements.
Other share-based compensation
The CEO and other members of the Corporate Management Board are eligible to participate in Hydro’s discounted employee share purchase plan on the same terms as all other eligible employees (as described in note 17 Employee remuneration).

Pensions
There are two pension plans in Hydro in Norway, defined benefit and defined contribution. The defined contribution plan was established on March 1, 2010 at the same time as the defined benefit plan was closed to new entrants. A cash compensation scheme has been established for employees who have been transferred from the defined benefit plan to the defined contribution plan and for whom a deficit in pension capital resulting from the transfer has been estimated.

As of January 1, 2017, approximately 78 percent of the employees in Norway, including five members of the Corporate Management Board, are members of the defined contribution plan. The rest, including the CEO and two members of the Corporate Management Board, are members of the defined benefit plan.

Following changes to the Norwegian National Insurance Scheme and the Act on Defined Contribution Occupational Pension, the company has adjusted its defined contribution plan. Effective January 1, 2017, payments into the plan equal 6 percent of salary between 0G and 12G, where “G” is the Norwegian National Insurance basic amount, and an additional payment of 14 percent of salary between 7.1G and 12G (for a total of 20 percent in this salary range.)

The defined benefit plan implies a pension right of approximately 65 percent of pensionable salary subject to full service period (minimum 30 years).

Effective January 1, 2017 the company has closed the 12G plan, which is the arrangement funded through operations for earning pension on the portion of any salary exceeding 12G. For employees with a defined contribution plan, an amount equivalent to 20 percent of the portion of salary exceeding 12G is allocated as a vested (pension) right. For employees with a defined benefit plan, the portion of salary exceeding 12G is included in the final salary that forms the basis for calculating pension. The closing of the 12G plan means that employees with salaries exceeding 12G as of December 31, 2016 remain in the plan, while employees with salaries below 12G on that date will not be included in the plan even if their salary later exceeds 12G. New employees, including new members of the Corporate Management Board (recruited internally or externally), will not be offered the possibility to earn pension on the portion of salary exceeding 12G. The CEO and the other Norwegian members of the Corporate Management Board were part of the 12G plan at the beginning of 2015 and therefore remain in the plan.

The company has adapted to the new rules on age limits in the Working Environment Act by implementing an internal company age limit of 70 years effective July 1, 2016. Implementation of a new age limit, combined with new flexible rules for pension withdrawals, means that Hydro in Norway no longer employs the concept of retirement age. In the company’s defined benefit pension plan, employees will continue to earn pension up until 67 years of age. The company has no early retirement plan, except for the two closed schemes described below.

Until 2011, Hydro had an early retirement scheme for employees at certain levels that offered a right to retire at the age of 65 with an entitlement to 65 percent of pensionable salary until the age of 67. All current Norwegian members of the Corporate Management Board were members of the scheme when it closed and are, thus, still covered by it.

In addition, the CEO has a right to retire, and the Board of Directors may require him to do so, after the age of 62 with an entitlement to 60 percent of pensionable salary until the age of 65. From the age of 65, the entitlement is 65 percent of pensionable salary (in accordance with the scheme described in the foregoing paragraph). Two members of the Corporate Management Board belong to an early retirement scheme that gives them the right to retire at the age of 62 with an entitlement to 60 percent of pensionable salary until the age of 65, subject to at least five years of service on the Corporate Management Board between the ages of 50 and 60. This scheme was discontinued in 2012.

The pensionable salaries of the CEO and of two members of the Corporate Management Board have been capped. The pensionable salary caps are subject to annual adjustment in accordance with the adjustment of the Norwegian National Insurance basic amount. Following the adjustment as of January 1, 2017, the pensionable salaries are capped at NOK 7,247,324 for the CEO and NOK 4,445,823 for the two members of the Corporate Management Board.
Insurance
The CEO and other members of the Corporate Management Board are covered by insurance arrangements applicable to all Hydro employees with a rank of vice president or higher.

Termination agreement
In the event the CEO’s employment is terminated before age 62 unilaterally by Hydro, the CEO has a contractual right to a notice period of six months, plus severance pay and other remuneration (excluding bonus and LTI payments) for 12 months but not beyond the age of 62. Two members of the Corporate Management Board have a similar arrangement as the CEO, but without the limitation of 62 years. Other Norwegian members of the Corporate Management Board have, as of the beginning of 2017, a contractual right to a notice period of six months, plus six months’ severance pay.

The CEO’s contract and the contracts of the two members of the Corporate Management Board referred to above give the company the right to reduce severance pay in the event of new regular income.

The CEO’s employment contract contains provisions on the loss of severance pay if there are grounds for summary dismissal. Other employment contracts include provisions on the loss of severance pay for gross breach of duty or other material breach, and subsequent termination of employment on such grounds. None of the contracts gives the right to severance pay if the employee has initiated the termination of employment.

The company has no specific guidelines for severance packages, but when recruiting for corporate management in recent times, it has followed a practice whereby the total of salary during the notice period and severance pay does not exceed 12 months’ salary.

Members of the Corporate Management Board outside Norway
For members of the Corporate Management Board outside Norway, base salary and other employment conditions are determined in accordance with Hydro’s global human resources policy and local industry standards, and accords generally with the remuneration principles applicable to the other members of the Corporate Management Board.

The former head of Hydro’s Bauxite & Alumina business area, Alberto Fabrini, resigned in October 2016. His successor Silvio Porto, who took over on December 13, 2016, is (as Fabrini was) employed by Norsk Hydro Brasil Ltda. and has variable compensation schemes deviating from the description above. These schemes entail a framework for variable compensation of just over 9 months’ base salary for each of a short-term incentive and long-term incentive. Both incentive schemes are performance-based as described above. The Board of Directors’ overall assessment is that Porto’s total remuneration framework is in accordance with market practice in Brazil.

Porto is covered by the share-based long-term incentive (LTI) plan described above on the same terms as the Norwegian members of the Corporate Management Board.

Key principles for determining compensation during the previous financial year
The compensation of the CEO and the other members of the Corporate Management Board for the financial year 2016 was based on the guidelines presented at the Annual General Meeting in 2016.

In July 2016, the Board of Directors decided to increase the CEO’s base salary by 2.5 percent, from NOK 6,065,000 to NOK 6,217,000 effective January 1, 2016.

Bonus payments for 2015 were determined and paid in 2016 on the basis of the principles described above (see also Note 9 Management remuneration). Bonus payments for 2016 were determined in March 2017 on the basis of the principles described above and will be paid during 2017.