

**Report of the Board of Directors  
on the proposals for the compensation  
of the Board of Directors  
and of the Executive Board**



of Good Food, Good Life



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## Overview

This Report informs the shareholders of Nestlé S.A. on the proposed maximum compensations of the Board of Directors and of the Executive Board submitted to the shareholders for approval at the Annual General Meeting of 6 April 2017.

## I. Governance Framework

At the Annual General Meeting of 10 April 2014 the shareholders approved the revision of the Articles of Association to incorporate and transpose new requirements of Swiss Company law, including the new power of the General Meeting to approve the compensation of the Board of Directors and of the Executive Board in a binding vote. Nestlé's Articles of Association were amended to include comprehensive provisions regarding the structure and basic principles of the compensation of the Board of Directors and of the Executive Board which meet best corporate governance and compensation practices (art. 21<sup>bis</sup> to art. 21<sup>quater</sup>).

Pursuant to the Articles of Association, the Board of Directors shall submit at the forthcoming Annual General Meeting the proposed maximum compensation separately for the Board of Directors, for the period from the Annual General Meeting 2017 to the Annual General Meeting 2018 (Agenda item 5.1), and for the Executive Board for the business year 2018 (Agenda item 5.2). This Report explains the related proposals of the Board of Directors.

In addition to their vote on the maximally possible compensation amount for the Board of Directors and the Executive Board, shareholders can at subsequent Annual General Meetings retrospectively vote on the Compensation Report including the actual compensation pay-out (advisory vote).

## II. Approvals of the Annual General Meeting 2016

At the Annual General Meeting of 7 April 2016 the shareholders approved with strong majorities a maximum compensation for the Board of Directors of CHF 10.5 million for the period from the Annual General Meeting 2016 to the Annual General Meeting 2017, and a maximum compensation of CHF 60 million for the Executive Board for the business year 2017.

For the period from the AGM 2016 to the AGM 2017, the actual compensation pay-out for the Board of Directors was CHF 10.0 million, below the approved maximum of CHF 10.5 million. The actual compensation pay-out for the Executive Board was CHF 51.9 million for the business year 2016, below the maximum of CHF 60 million approved by the shareholders on 16 April 2015.

In addition, the shareholders accepted the Nestlé Compensation Report 2015 in a separate advisory vote, with a strong majority.

### III. Proposals to the Annual General Meeting 2017

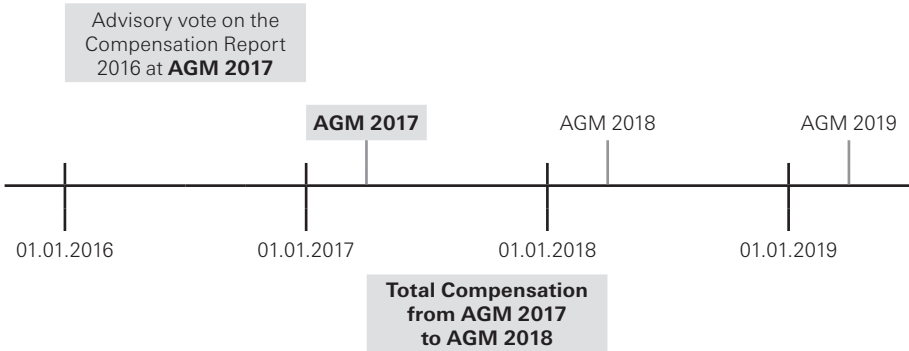
#### 1. Compensation of the Board of Directors (Agenda item 5.1)

##### Proposal

Approval, prospectively, for the period from the Annual General Meeting 2017 to the Annual General Meeting 2018, of a **total compensation for the 13 non-executive members of the Board of Directors** (including the Chairman, but excluding the CEO) of **CHF 10.0 million**, including CHF 4.0 million in cash remuneration, CHF 5.5 million in Nestlé S.A. shares blocked for a 3-year period (discounted by 16% to account for the blocking period of 3 years) and CHF 0.5 million for social security contributions and other fees.

##### Explanation

Timeline:



The remuneration of the members of the Board of Directors is set to attract and retain highly qualified individuals to serve on the Board of Directors. The level of remuneration reflects the time and effort required from the members in fulfilling their Board and Committee responsibilities. The pay structure (cash and blocked Nestlé S.A. shares) is designed to ensure the Board's focus on the long-term performance and success of the Company.

With the exception of the Chairman and the CEO, each member of the Board of Directors receives a Board membership fee of CHF 280 000 and an Expense Allowance of CHF 15 000. These figures have remained unchanged since 2006.

Members of a Board Committee receive the following additional fees <sup>(a)</sup>:

	Chair	Members
Chairman's and Corporate Governance Committee	CHF 300 000	CHF 200 000
Compensation Committee	CHF 150 000	CHF 70 000
Nomination and Sustainability Committee	CHF 100 000	CHF 40 000
Audit Committee	CHF 150 000	CHF 100 000

(a) The Chairman and the CEO Committee fees are included in their total remuneration.

The above fees and allowances cover the period between the Annual General Meeting 2017 and the Annual General Meeting 2018. Board membership and Committee fees are paid 50% in cash (in two half-yearly instalments) and 50% in Nestlé S.A. shares, which are subject to a three-year blocking period.

Additional fees are paid to two members of the Board of Directors who serve as members of the Creating Shared Value (CSV) Council (CHF 25 000 each), and to one member of the Board of Directors who serves on the Steering Committee of the Nestlé Institute of Health Sciences (CHF 10 000).

The Board of Directors has decided to propose Mr Paul Bulcke for election by the shareholders as Chairman. In his capacity as active, non-executive Chairman, Paul Bulcke, if elected, will receive - as all other non-executive members of the Board of Directors - a cash compensation as well as Nestlé S.A. shares, which are blocked for three years. The Chairman's remuneration reflects certain responsibilities for the direction and control of the Group including the support of the new CEO, the support of Nestlé Skin Health and Nestlé Health Sciences through the respective Strategic Advisory Boards and the direct leadership of Nestlé's interests in L'Oréal. Mr Bulcke will also chair the 2030 Water Resource Group (WRG), and represents Nestlé as member of the European Roundtable of Industrialists (ERT), and as member of the WEF International Business Council. The proposed remuneration includes all compensation received in relation to these activities.

5-year history of Board of Directors compensation (including company contributions to social security)<sup>(a)</sup>:

2012	CHF	12.1 million
2013	CHF	12.1 million
2014	CHF	11.3 million
2015	CHF	10.8 million
2016	CHF	10.0 million

(a) For details, please refer to the Compensation Report of the relevant business year.

While the evolution of the above figures is affected by changes in the compensation structure and number of Board members, the relative stability in ongoing costs reflects that Board membership fees and expense allowances have remained unchanged since 2006.

The 2016 budget of CHF 10.5 million (approved at the AGM 2016) and the proposed 2017 budget of CHF 10.0 million are in line with the 5-year compensation history.

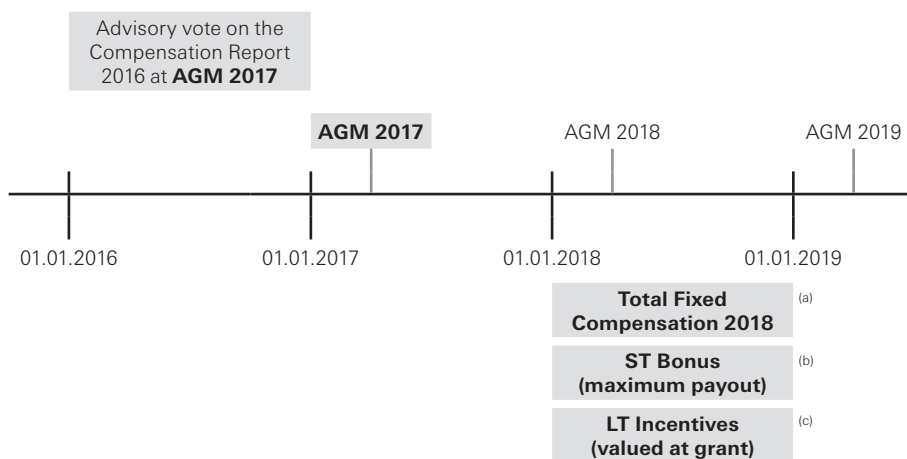
## 2. Compensation of the Executive Board (Agenda item 5.2)

### Proposal

Approval, prospectively, for the period from 1 January 2018 to 31 December 2018, of a **total maximum amount of compensation for the 14 members of the Executive Board, including the CEO, of CHF 60 million**, including CHF 16 million for base salary, CHF 20 million for short-term bonus (based on maximum target achievement, discounted in the case of the CEO by 16% for the 50% paid in blocked Nestlé S.A. shares), CHF 16 million for long-term incentive plans (based on fair value at grant), CHF 4 million for contributions for future pension benefits and CHF 4 million for social security contributions, other benefits and unforeseen expenses.

### Explanation

Timeline:



- (a) Annual Base Salary + Pension & other benefits
- (b) Short-Term Bonus based on 2018 performance
- (c) Long-Term Incentives granted in 2018

Mr Mark Schneider was appointed CEO as from 1 January 2017. Together with Paul Bulcke, who is highly experienced in the area of fast moving consumer goods and whom the Board of Directors proposes for election as Chairman, the new team is ideally suited to ensure the long-term strategic direction of the Company set by the Board of Directors whilst fostering Nestlé's values and principles.



The Total Compensation for the members of the Executive Board includes a fixed portion (Annual Base Salary) and a variable portion (Short-Term Bonus and Long-Term Incentives). Both fixed and variable compensation are determined in line with collective and individual performance.

Compensation for members of the Executive Board is aligned with long-term company strategy and shareholders' interests. The Short-Term Bonus pay-out is determined by the degree of achievement of a number of annual operating objectives. Long-Term Incentives are provided in the form of share-based instruments, therefore ensuring alignment with shareholders' interests.

The Board values compensation proposals according to the valuation principles applied to and indicated in the Compensation Report. Conditional benefits are valued at the date of grant, using where applicable generally accepted valuation models to determine the fair value at grant.

### **Short-Term Bonus**

The Short-Term Bonus is expressed in % of the Annual Base Salary.

The target levels are:

– CEO	150%
– Executive Vice Presidents	100%
– Deputy Executive Vice Presidents	80%

For the CEO, 100% of the target is linked to Nestlé Group performance. For the other members of the Executive Board, at least 50% of the target is linked to business performance, to ensure accountability for Nestlé's results: for Function Heads, 50% is tied to Group performance, 30% to functional objectives and 20% to their individual performance (quantitative and qualitative objectives); for Zone or Business Heads, 30% is tied to Group performance, 50% to business goals they are directly responsible for, and 20% to individual performance (quantitative and qualitative objectives). In case an Executive Board member reaches all his/her objectives in full, the bonus pay-out will correspond to the above-mentioned targeted level. If one or more objectives are not reached, the bonus is reduced. There is no guarantee for a minimum pay-out of the bonus. On the other hand, the bonus pay-out is capped at a maximum of 130% of the target. Over-performance of members of the Executive Board can thus be rewarded with a pay-out exceeding the target but will in no event exceed the 130% maximum level.

The objectives are set at the beginning of each year by the Board of Directors in line with the Company's strategy. The Nestlé Group performance is determined by the Board of Directors, based on measurable operational objectives, most importantly organic growth, real internal growth, operating profit, and cash flow generation. Additional objectives used to evaluate the Nestlé Group performance are related to the Nestlé strategic roadmap. The overall Group achievement level is fixed by the Board of Directors.

Individual objectives are determined by the CEO for each member of the Executive Board. They are related to the individual area of responsibility and can be of financial or non-financial nature depending on the respective function. The corresponding pay-out level is approved by the Compensation Committee.

Members of the Executive Board can elect to receive part or all of their Short-Term Bonus in Nestlé S.A. shares, which are blocked for a period of three years. The CEO has to take a minimum of 50% in shares.

### **Long-Term Incentives**

Members of Nestlé's Executive Board are eligible to receive Long-Term Incentives, in the form of Performance Share Units (PSUs) under the Performance Share Unit Plan (PSUP). The target grant values, expressed in % of the Annual Base Salary, are:

- CEO 150%
- Executive Vice Presidents and Deputy Executive Vice Presidents 100%

The Performance Share Unit Plan (PSUP) provides units which entitle participants to receive Nestlé S.A. shares at the end of a three-year vesting period following their grant. The level at which PSUs vest is determined by the degree by which the two performance measures of the PSUP have been met. These two criteria are:

- the relative Total Shareholder Return of the Nestlé S.A. share in relation to the STOXX Global 1800 Food & Beverage Net Return Index;
- the growth of underlying Earnings per Share in constant currencies.

The vesting range of the PSUP starts at 0% and is capped at 200% of the initial PSU award, thus providing alignment with long-term strategy and shareholders' interests.

The fair value of Long-Term Incentives at grant is determined by using generally accepted pricing models, taking into account the potential upside and downside impact of Company performance at the end of the three-year vesting period.

For members of the Executive Board, the Nestlé S.A. shares earned are submitted, in addition to the three-year vesting period, to an additional two-year holding period, during which they cannot dispose of their shares.

For the Head of Nestlé Health Science, the LTI target grant values are the same as above, but are split between PSUP (30% of grant value) and the specific Long-Term Incentive Plan of Nestlé Health Science (70% of grant value). Nestlé Health Science has a Phantom Share Unit plan based on the long-term development of that business, with a vesting period of three years, and a value capped at two times the Unit price at grant.

### **Pension benefits**

Executive Board members are affiliated to the Nestlé Pension Plan in Switzerland, like all other employees based in Switzerland. The employer's contributions for future pension benefits are included in the compensation amount. In addition, any part of the annual base salary which exceeds the ceiling prescribed by Swiss Pension law is covered directly by the Company.

### **Other benefits**

The Company limits other benefits to a minimum. Typical elements are a car allowance (there are no company cars provided to the members of the Executive Board), a contribution towards health insurance premiums (below CHF 4000 per annum for each Executive Board member) as well as long-term service awards in line with Company policy, as offered to other employees. Those Executive Board members who have been transferred to Switzerland from other Nestlé locations are eligible to receive benefits in line and within the limits of the Nestlé Corporate Expatriation Policy.

### **Maximum pay-out**

**The compensation proposal made by the Board of Directors to the shareholders reflects the maximum possible bonus pay-out. The maximum amount of CHF 60 million proposed to the Annual General Meeting 2017 remains unchanged vs. the maximum amount approved for 2017 by the shareholders at the Annual General Meeting 2016.**

The maximum possible pay-out assumes a 130% achievement of all bonus targets, both Company and individual, as well as a payment in cash of maximally reachable Executive Board bonuses. The detailed plans for 2018 are not yet available at this point in time. The maximum possible pay-out would require highly exceptional performance.

5-year history of Executive Board compensation (including company contributions for future pension benefits and for social security):

			Nestlé Group results achievement <sup>(a)</sup>
2012	CHF	51.2 million	117%
2013	CHF	50.7 million	95%
2014	CHF	50.6 million	101%
2015	CHF	54.5 million	93%
2016	CHF	51.9 million	95%

(a) Used to determine 100% of the CEO's bonus, and between 30% and 50% of the bonus of other Executive Board members.

As per above, the total compensation of Nestlé's Executive Board has been relatively stable over the past years.

The 2017 budget of CHF 60 million (approved at the AGM 2016) and the proposed 2018 budget of CHF 60 million allow for potential uncertainties such as the achievement of a maximum possible bonus pay-out.



**Nestlé**

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