

LOCAL EXPERTISE  
MEETS GLOBAL EXCELLENCE

2010

Remuneration report 2010 pursuant to  
the German Ordinance governing supervisory  
requirements for remuneration systems of institutions  
(Instituts-Vergütungsverordnung)



**Aareal Bank  
Group**

# Remuneration report 2010

## Information and disclosure under the "Ordinance governing supervisory requirements for remuneration systems of institutions" (InstitutsVergV)

### New requirements for banks' remuneration systems

On 13 October 2010, the German ordinance governing supervisory requirements for remuneration systems of institutions (InstitutsVergV) went into force. It replaces the provisions governing compensation contained in the BaFin circular (RS 22/2009) dated 21 December 2009. This ordinance places requirements upon the remuneration systems of credit institutions. Those requirements have necessitated a review of the existing Aareal Bank AG remuneration system. The bank has involved external consultants in adapting its compensation structures to the new requirements. In so doing, the basic structure of the system to date was retained.

The following group-wide remuneration principles underlie the modified remuneration system that went into effect on January 1, 2011:

- transparent remuneration models geared to sustainability
- assurance of an attractive and motivating remuneration with the aim of procuring and retaining highly-qualified personnel
- avoidance of identical parameters for the level of the variable employee remuneration of the control units and of the organisational entities that they supervise, which could lead to possible conflicts of interest.
- avoidance of incentives for taking disproportionately high risk positions
- fulfilment of regulatory requirements

The overriding goal is to gear the remuneration to the market, to performance and to the profitability of the corporation as well as to address the interests both of the employees, the management and shareholders and to ensure the sustainable upward growth of Aareal Bank.

### The remuneration system of Aareal Bank AG

The compensation models tailored to the various employee groups constitute the core of the modified remuneration system. The bank uses these models to ensure payment of compensation that is profit-, performance- and risk-driven.

These models are discussed below. The remuneration models for managers and for employees whose work has a material influence on the overall risk profile of the bank (risk takers) rest upon the employee remuneration model.

## **1.) Remuneration model for employees**

The employee remuneration has fixed and variable components.

The framework for setting market- and performance-driven compensation is a position plan. For salary scale employees, it differentiates between the different salary scale levels and for off-salary scale employees, between four levels in the expert career path and three in the management career path. All employees are classified in this position plan according to the requirements of their positions. Salary bands for fixed remuneration are allocated to the position levels. The salary of salary scale employees is governed by their allocation to one of nine salary scale groups and the number of years worked. The fixed salary of the off-salary scale employee is determined such that is both in line with the market and appropriate with regard to the scope of responsibility and individual requirements of the position in question. A review of the annual fixed remuneration paid out in twelve monthly instalments is performed annually.

All employees can receive variable remuneration normally paid with the April salary. The aim of that is to remunerate individual performance in line with the market and performance and bank profits, beyond the fixed compensation. In this procedure, target figures are set for the variable compensation of all staff. The position plan of the bank defines upper thresholds for the relationship between remuneration varying according to the achievement of sustainable profitability on the one hand and total remuneration on the other; the paid variable remuneration may not exceed 200% of the target figure.

The actual level of the individual variable remuneration for salary scale employee depends on the individual performance appraisal by the supervisor responsible. For off-salary scale employees it also depends on the achievement of individual targets previously agreed upon.

The Management Board sets lump-sum markups or markdowns to boost or cut the variable remuneration set by the managers. The level of those increases or haircuts depends on the level of the bonus pool available. The same add-on or discount factors are used across the board for all employees.

In the cases provided for in section 45 German Banking Act, the Management Board of Aareal Bank AG may reduce and - if applicable - reduce to zero - the bonus pool of Aareal Bank AG if up to the publication of the annual report for the respective year under review, the bank's equity capital does not meet the requirements of section 10, para. 1 or 1b, or of section 45b, para.1 German Banking Act, or if the investment of the bank's funds does not meet the requirements of section 11, para. 1 German Banking Act, or if the bank's assets, earnings or financial development justifies the assumption that the bank will be unable to meet those requirements in the long term.

## **2.) Remuneration model for Executive staff**

The total remuneration for executive staff is made up of fixed remuneration paid in twelve monthly instalments and variable remuneration, the so-called total incentive. The total incentive is made up of a cash component (bonus) and a stock component in the form of so-called virtual shares.

At the beginning of a year under review, the target values for the variable remuneration (target total incentive) are fixed for all Senior Managers individually. These target total incentives may not exceed a ceiling of 40 % of individual total remuneration. The Management Board determines the bonus pool for the relevant financial year after the end of the year under review. That determination is based on the corporate performance and the sum of the target total incentives. The actual amount of the individual total incentives is

determined on the basis of the individual contributions to performance, such contributions being composed of the attainment of the individually-agreed targets and a general performance assessment. To assess the individual contributions to performance, five appraisal grades are used: they cite the range within which the actual total incentive may fluctuate as a ratio of the target total incentive.

The shares of the cash component and the share component in the total incentive are determined individually by the Management Board. As a general rule, the proportion of the virtual shares should not exceed one-third of the total incentive.

Whereas the cash component is usually paid out along with the April salary (bonus payment date) in the year after the measurement period, the payout of the share component occurs annually over a period of 3 years at one-third each starting in the next year but one after the period under review. The senior manager can determine, at fixed dates during a 3-year period, the actual payment date of each tranche after expiry of the deferral period.

### **3.) Remuneration model for employees and Executive staff whose activity under InstitutsVergV makes them risk takers**

In its risk analysis, Aareal Bank has identified risk takers whose work has a material influence on the overall risk profile of the bank. This group of risk takers includes especially employees of the management level directly below the Board; managers in the sales units of Structured Property Financing and members of bank committees that are central.

After fixed remuneration paid out in twelve monthly instalments these risk takers receive variable compensation (total incentive) made up of the following four components:

- Cash Bonus
- Share Bonus
- Restricted Cash Award (RCA).
- Restricted Virtual Share Award (RVSA)

At the beginning of the year under review, the target values for the variable remuneration (= Target Total Incentive) are fixed for all risk takers individually. As a matter of policy, the individual Target Total Incentives of risk takers must not exceed a ceiling of 45 % of individual total remuneration. The actual level of the individual Total Incentives is determined analogous to the remuneration model for the Executive staff.

Risk takers who give the Board particular support on strategic questions have a direct claim on variable compensation in the amount of 40 % of the individual Total Incentive at the end of the period under review, other risk takers 60 %, of which

- 50% in the form of a cash component (Cash-Bonus). The cash bonus is paid out in the year after the end of the period under review.
- 50 % in the form of a share bonus. The share bonus is paid out after a deferral period of two years following on the origination of the claim. The claimant may defer the payout date by a maximum of three years on the basis of an option right.

Risk takers who give the Board particular support on strategic issues get 60 % of individual Total Incentives merely announced to them, and other risk takers 40%, of which

- 50% as Restricted Cash Award (RCA). The claim on this RCA arises over a period of 3 years in the amount of one-third each starting a year after the start of the period under review and subject to adherence to the malus provision (see below) The payout of the RCA occurs at the time the claim arose.
- 50 % in the form of a share component (Restricted Virtual Share Awards - RVSA). The claim to this RVSA also arises over a period of three years in the amount of one-third each starting a year after the start of the period under review and subject to adherence to the malus provision (see below). The payout on the RVSA occurs after a deferral period of one year as from the time the claim arises. The claimant can delay the payout date by a maximum of three years on the basis of an option right.

#### **Malus provision (penalty-triggering events)**

If the profit for the year allocated to Aareal Bank AG shareholders after adjustment for one-off effects for the year preceding the payout year should be negative, the payout of the one-third of the RCA awaiting disbursement is waived. The bank is further entitled to reduce the level of the RCA and RVSA tranches appropriately or to waive them entirely if the bank's equity capital does not meet the requirements of § 10, section 1 or section 1b, or of § 45b, section 1 German Banking Act, or if the investment of the bank's funds does not meet the requirements of § 11, section 1 German Banking Act, or if the bank's asset, earnings or financial development justifies the assumption that the bank will be unable to meet those requirements in the long term.

In the event of serious individual misconduct in the period up to the origination of the claim, which is discovered afterwards, the amount of those tranches in relation to which a claim has not yet arisen may be appropriately reduced or entirely waived. Examples of such severe individual infringements are:

- misconduct which justifies immediate dismissal of the employee
- a violation of the ban on hedging
- a material infringement of internal guidelines

The same applies when the bank becomes aware at a later date of circumstances on the basis of which the individual employee performance used to measure the variable remuneration would be classed in retrospect in the worst assessment grade defined in the appraisal system.

#### 4.) Remuneration of Management Board members

The Board members are remunerated according to individual agreements. The details on this and the appertaining remuneration information were published in the annual report 2010 (p. 205 ff.).

### The Remuneration Committee

The Aareal Bank Remuneration Committee that had existed since 15 December 2009 was reworked once the requirements placed upon such committees by InstitutsVergV took effect. The committee has the job of monitoring the appropriateness of the remuneration systems and of reporting to the Management and Supervisory Boards on this. It includes representatives both of organisation units that initiate business and of those that monitor them.

Internal Audit is included in the work of the committee according to its tasks.

### Disclosure of remuneration indicators under InstitutsVergV

The disclosure under section 7 InstitutsVergV includes the remuneration for all staff for 2010<sup>1</sup> and is made below for Aareal Bank AG and for its subsidiaries as defined under section 10a German Banking Act, where these are subject to InstitutsVergV.

#### Remuneration information under section 7 InstitutsVergV

€ mn	Structured Property Financing	Consulting / Services	as a whole
Total remuneration	90.9	11.8	102.7
of which: fixed remuneration	63.4	9.7	73.1
of which: variable remuneration for 2010	27.5	2.2	29.6
No. of beneficiaries	(966)	(168)	

After entry into force of InstitutsVergV and the classification of Aareal Bank under section 1(2) InstitutsVergV as a significant bank, the work contracts of the risk takers so identified were able to be converted only as from 1.1.2011. So the disclosure of remuneration indicators under section 8 InstitutsVergV will occur for the first time in 2012 for the year 2011.

<sup>1</sup> Excluding Management Board of Aareal Bank AG (see here annual report 2010, p. 205 ff.)

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