Courtesy Translation
of the draft letter to the Government Commission
on the German Corporate Governance Code

Code reform 2019
Joint comment by the Executive Board and the Supervisory Board of K+S Aktiengesellschaft

Dear Professor Nonnenmacher,
Dear Sir or Madam,

On 6 November 2018, you published the draft of an amended Code and invited the interested public to comment upon the proposed Code amendments until 31 January 2019. We would therefore like to submit this joint comment by the Supervisory Board and the Executive Board of K+S Aktiengesellschaft.

We explicitly support the objectives of the Government Commission, i. e. “enhanced relevance, clearer and more compact wording”. Our comments upon structure as well as on the recommendations and suggestions respectively aim to follow these objectives.

I. Structure

According to section 161 Stock Corporations Act (which forms the basis for the Code) Executive Board and Supervisory Board of a publicly listed stock corporation explain once a year that they have complied/will comply with the recommendations of the Code and which recommendations were not complied with and why (“comply or explain”). Section 161 Stock Corporations Act forms the legal basis for the Code and for the declaration of conformity. Both Code and declaration of conformity are integrated in the overall legal framework. The provision does not give any competency to developing the law.

Against this background a recommendation going beyond the declaration of conformity (cf. part 1 below) or an anticipation of possible future legal provisions (cf. part 2 below) are not covered by section 161 Stock Corporations Act.

1. Recommendation going beyond the declaration of conformity

The draft recommendation A. 19 stipulates that the Supervisory Board and Executive Board shall explain how they apply the principles of the Code (“apply and explain”). The “apply and explain” approach, which is intended as a further level of the Code, is not covered by the Stock Corporations Act.

Essential reporting medium is the declaration of Corporate Governance according to section 289f Commercial Code, which has to be set up by the Executive Board as a separate section of the management report and which has to be surveyed by the Supervisory Board (and the auditor respectively) according to section 171 subsection 1 sentence 1 Stock Corporations Act.

The draft recommendation A. 19 requires a joint explanation by the Executive Board and the Supervisory Board, which conflicts with this legal systematics.

The “principles of the Code” shall form the basis of the explanation. According to paragraph 4 of the foreword the principles *reflect* both significant legal requirements and fundamental standards of good and responsible governance.

The Code must not be used to modify the legal provisions via the declaration of conformity according to section 161 Stock Corporations Act. The principles, recommendations and suggestions of the Code have to be consistent with the legal provisions.

The declaration according to section 161 is well established. It forms a fundamental basis for a lot of different operational transactions. A full declaration of conformity is often mandatory prerequisite for those transactions, the model of “comply or explain” does not really work in practice.

Recommendations of the Code that go beyond legal provisions lead to an indirect modification of the respective legal provisions. This is not covered by section 161 Stock Corporations Act and is questionable under constitutional law.

Some of the Code principles relate to aspects that are reflected in the articles of association or the bylaws of the Executive or Supervisory Board. An explanation would be limited to a reference to those documents without additional knowledge production.

In an increasingly complex surrounding we would appreciate waiving any such additional reporting requirements. In any case, those reporting requirements have to be consistent with the legal reporting requirements.

2. Anticipation of possible future legal provisions

The draft Code refers to possible future legal provisions for the implementation of the second directive on shareholders rights and summarizes them in an inaccurate way as principles of the Code. With regard to the legal systematics described above such an anticipation of possible future legal provisions finds no legal basis in section 161 Stock Corporations Act.

II. Principles, recommendations and suggestions

1. Principle 11

Principle 11 – according to which material transactions with related parties are subject to prior approval of the Supervisory Board – summarizes an anticipation of possible future amendments according to sections 111a – 111c Stock Corporations Act as amended by the draft law for the implementation of the second directive on shareholders rights (AktG-E ARUG II). This summary leads to a possible conflict with the legal provisions.

Intra-group exemptions according to section 111a AktG-E ARUG II as well as possible threshold values according to section 111b subsection 1 AktG-E ARUG II are not reflected in principle 11. Contrary to principle 11, a prior consent of the Supervisory Board would not be required in those cases.

The Code does not comment upon a possible committee of the Supervisory Board (according to section 107 subsection 3 AktG-E ARUG II) responsible for the preparation of resolutions of the Supervisory Board on the consent to material transactions with related parties.

2. A. 13

The draft Code recommends that the Supervisory Board shall meet on a regular basis without the Executive Board. Without further clarification, this recommendation could lead to a conflict of the Supervisory Board members between compliance with their declaration of conformity and compliance with their respective mandatory legal obligations. According to section 111 subsection 1 Stock Corporations Act the Supervisory Board has to control the management. The standard of section 93 Stock Corporations Act applies to this control (cf. section 116 sentence 1 Stock Corporations Act). Section 93 subsection 1 sentence 2 Stock Corporations Act requires actions based on adequate information. The Executive Board is responsible to provide the information to the Supervisory Board as further described in section 90 Stock Corporations Act. Actually, the Supervisory Board regularly meets in the presence of the Executive Board in order to fully comply with the legal requirements.

It might be possible to have preliminary meetings on a regular basis without the Executive Board, however, the plenary meetings of the Supervisory Board shall take place with the Executive Board being present.

3. A 15

The draft recommendation A. 15 stipulates that the Supervisory Board shall assess, at regular intervals, how effective the Supervisory Board as a whole and its committees fulfill their tasks. This self-assessment shall be supported by external resources after not more than three years.

It could be considered to extend the periods according to sentence 2 of the draft to four years. This would enable the Supervisory Board to an internal self-assessment every two years in between. In principle, it should be noted that the provision of external support should not incur significant additional costs for the company. This would also argue in favor of extending the interval between external support to four years.

4. A. 23

Besides the mandatory legal obligations and the agreements with the auditors according to recommendations A. 21 and A. 22, draft recommendation A. 23 (evaluation of the effectiveness of the audit on a regular basis) lead to an additional bureaucratic burden without additional knowledge production. There are numerous

duties of the Supervisory Board and the Audit Committee with regard to the election of and the collaboration with the auditors. With regard to the objectives of the Code, this recommendation should be deleted.

5. B. 1

There is no apparent reason, why Supervisory Board members elected by the shareholders shall not be appointed for a period of more than three years in accordance with the draft recommendation B. 1. This recommendation limits section 102 subsection 1 Stock Corporations Act, the Code leads to a modification of the legal provisions.

Furthermore, the draft recommendation B. 1 would mean a (not justified) inequality between the Supervisory Board members elected by the shareholders and those elected by the employees on the basis of the Co-Determination Act.

6. B. 5/B. 6

The proposed recommendations would modify the legal provision of section 100 subsection 2 Stock Corporations Act, the Code would modify the legal provisions. The draft Code recommends that a Supervisory Board member who is not a member of any executive governing body of a third-party entity shall not accept more than five Supervisory Board mandates at listed companies or comparable functions, with an appointment as Chair of the Supervisory Board being counted twice. According to the draft recommendation B. 6, members of the executive governing body of a third-party entity shall not have, in aggregate, more than two Supervisory Board mandates in non-group listed companies or comparable functions, and shall not accept the Chairmanship of a Supervisory Board.

Section 100 subsection 2 Stock Corporations Act adequately reflects the requirements for a diversified and competent Supervisory Board. The restrictions proposed by the draft recommendations B. 5 and B. 6 would weaken the possible competency profile of the Supervisory Board.

Furthermore, according to section 101 subsection 1 sentence 2 Stock Corporations Act, the General Meeting is not bound to the election proposals by the Supervisory Board so that the Supervisory Board cannot make sure to comply with the own declaration of conformity. A cautious Supervisory Board would have to disclose and explain a departure justified by the mandatory legal provisions, as the Supervisory Board could not make sure to fully comply with the Code.

7. Principle 22

According to the draft of principle 22, the Supervisory Board resolves upon the number of Executive Board members, the allocation of responsibilities, the required qualifications as well as the appointment of individual positions by suitable candidates, and takes into account the required diversity.

The draft of this principle 22 illustrates the problem of the summary of legal provisions. Principle 22 must not lead to a restriction of section 77 subsection 2 Stock Corporations Act.

8. Principle 23

Draft principle 23 deviates in four aspects from a possible future legal provision in section 120a subsection 1 AktG-E ARUG II. According to section 120a subsection 1 AktG-E ARUG II the General Meeting adopts a resolution on the *approval* of the remuneration *politics* for the Executive Board *provided* by the Supervisory Board *every four years*.

According to draft principle 23 sentence 2, the General Meeting adopts *advisory resolutions* on the approval of the remuneration *system* for the Executive Board members *suggested* by the Supervisory Board. There is no reason, why the Code deviates from the wording of a possible future legal provision. The General Meeting cannot adopt an advisory resolution. The resolution can only be adopted or not be adopted. Furthermore, there is no reason, why principle 23 does not reflect the possible future four year period.

9. D. 2

According to draft recommendation D. 2, the amount of remuneration shall be capped by annual maximum expense levels, both in aggregate and as regards variable remuneration components.

Compiling the annual maximum expense levels will not be possible, if the long-term variable remuneration is granted in the form of shares according to recommendation D. 7. It is impossible to follow recommendations D. 2 and D. 7 at the same time, so that the company would be forced to explain a departure for any of the two recommendations.

10. D. 3

The draft recommendation D. 3, according to which the service cost or pension contributions shall be allocated to the fixed remuneration category, leads to a false image.

11. D. 4

The draft recommendation D. 4 stipulates that the ratio between fixed remuneration and variable remuneration components shall take into account the various requirements related to the tasks of the respective Executive Board members.

The draft recommendation is contradictory to the principle of overall management by all members of the Executive Board according to section 77 subsection 1 sentence 1 Stock Corporations Act.

12. D. 5

The draft recommendation D. 5 stipulates that the amounts of all variable remuneration components granted shall depend solely upon the achievement of the pre-determined objectives for the period concerned.

Without further explanation, the reference to the pre-determined objectives limits the discretion of the Supervisory Board to adequately react to any occurrences during the year.

13. D. 7

The draft recommendation D. 7 stipulates that the short- term variable remuneration shall be granted (after deduction of taxes) in the form of shares in the company that must not be sold for a period of at least four years.

This draft recommendation leads to a limitation of the right of the Executive Board members to dispose of their remuneration that goes beyond the legal provisions and cannot be justified by law. Being a member of an Executive Board becomes less attractive to possible candidates. The Code weakens the Stock Corporations Act and the business location Germany.

In this context it has to be taken into account that the long-term variable remuneration shall exceed the share of short-term variable remuneration according to draft recommendation D. 1.

In addition, difficulties may arise in the simultaneous implementation of recommendation D. 12 which also relates to variable remuneration.

Lastly, the draft recommendation could lead to a potential conflict with the provisions of capital markets law (e. g. Regulation (EU) No 596/2014 on market abuse). Against this background, the recommendation needs to be substantiated.

14. D. 8

Draft recommendation D. 8 does not describe in detail how to compose the peer-group for the comparison. The composition of an adequate group for the comparison could be difficult or even impossible for K+S Aktiengesellschaft, if the peer-group was defined too narrow. It seems questionable, whether the objective of draft recommendation D. 8 can be achieved anyhow.

15. D. 12

Even if it seems reasonable to want to introduce “claw back” clauses, we would like to point out that the introduction of such clauses – as stipulated in the draft recommendation D. 1 – would lead to an increase in the remuneration of the Executive Board. In the case of K+S, which has so far pursued a very moderate remuneration

policy, this would mean a mandatory increase in the remuneration of the Executive Board.

16. D. 13

This draft recommendation, that any existing regulations regarding remuneration and the inflow of funds, limits the discretion of the Supervisory Board in case of a termination of a contract with a member of the Executive Board.

The termination of a contract with a member of the Executive Board always requires a decision by the Supervisory Board taking into account all circumstances of the individual case. Against this background, the Supervisory Board should be free to decide (within the bounds of the discretion).

If the contract with a member of the Executive Board is terminated, it is (internally and externally) often advisable to terminate all contractual relationships short-term. The payment of future remuneration would let a member leaving the Executive Board participate in future positive developments of the company without having contributed to and being responsible for this positive development.

17. D. 14

A severance payment, as described in the draft recommendation D. 14, remunerates the member leaving the Executive Board for the remaining term of the contract. The member leaving the Executive Board might have a legal claim that cannot be linked to a post-contractual restraint. Such post-contractual restraint has to be remunerated separately based on mutual consent. The draft recommendation D. 14 sentence 3, that payments made in return for possible post-contractual non-competition clauses shall be offset against the severance payment, cannot be unilaterally enforced.

18. D. 15

Under the terms of the draft, benefits in the event of a change of control should no longer be agreed. The aim of giving the Executive Board security and room to defend itself against takeover attempts, which are regarded as detrimental to the company, would be abandoned with such a clause. From this perspective, benefits in the event of a change of control helps the Executive Board to objectively assess an attempted takeover in accordance with the legal requirements.

We would highly appreciate if you considered the aspects listed above when further revising the Code.

Kind regards,

K+S Aktiengesellschaft

On behalf of the Executive Board	On behalf of the Supervisory Board
Dr Burkhard Lohr	Dr Andreas Kreimeyer