

Management compensation report

The management compensation report describes the principles applied when establishing the compensation to be awarded to members of the Executive Board and Supervisory Board of MTU Aero Engines AG, and states the amount and composition of that compensation. The management compensation report follows the provisions of Section 314 (1) no. 6 of the German Commercial Code (HGB), German Accounting Standard DRS 17 “Reporting on the remuneration of members of governing bodies,” the recommendations of the German Corporate Governance Code (GCGC), and the International Financial Reporting Standards (IFRSs).

At the proposal of the Personnel Committee, the Supervisory Board decides on a system of compensation for the members of the Executive Board, including the main components of their contracts, and reviews this system at regular intervals. In the interests of greater transparency and in accordance with revisions to the GCGC, the Supervisory Board passed a resolution in 2015 to modify the compensation system for members of the Executive Board as of the financial year 2016, because until now it included a relatively low proportion of share-based payments.

Variable compensation including long-term components

The present compensation system is commensurate with market conditions and aligned to the company’s performance. The variable compensation is oriented toward the company’s sustainable and positive development and includes a high proportion of share-based payments.

For a full description of the previous compensation system, in place until the end of 2015, please refer to the management compensation report in the Annual Report 2015.

Members of the Executive Board did not receive any compensation for mandates on boards of MTU group companies, nor were they granted any loan facilities by the company.

Principles of the compensation system for members of the Executive Board

At the proposal of the Personnel Committee, the Supervisory Board determines both the total compensation to be awarded to members of the Executive Board (total target direct compensation) and the composition of this compensation. The total target direct compensation is made up to around 40% of non-performance-related components, with the remainder being performance-related.

Non-performance-related components

The non-performance-related components consist of the basic salary (fixed compensation) and other benefits (fringe benefits) that are paid on a monthly basis. Fringe benefits comprise taxable reimbursements of expenses and the noncash benefit deriving from payments in kind such as insurance premiums and the use of a company car for business and private purposes, including any taxes on such benefits paid by the company.

Performance-related components

The performance-related components consist of the Annual Performance Bonus (APB) and the Restricted Stock Plan (RSP).

Performance-related components without long-term incentive effect

The Annual Performance Bonus (APB) is granted as a performance-related component without long-term incentive effect. It makes up around 40% of the variable portion of the target direct compensation.

The actual amount depends on the results achieved as regards two company performance targets and on the board member's individual performance. The company performance targets consist of the key performance indicators at group level – adjusted EBIT and free cash flow – which are given equal weighting. The targets to be achieved to ensure payment of 100% of the APB are set annually in advance by the Supervisory Board, taking the annual planning figures into account. In addition, an entry threshold below the planned level is set for each performance target; this corresponds to an APB entitlement of 50%. Should this entry threshold not be met, no short-term compensation shall be payable. Similarly, the maximum APB entitlement of 180% is payable if the maximum goal achievement level is reached in respect of the targets set for each of the two performance indicators. Between the entry threshold, the 100% level, and the maximum goal achievement level, the APB entitlement is interpolated using a straight-line method. The effective APB entitlement is calculated on the basis of the arithmetical mean of the levels achieved in respect of the two performance targets. In the case of adjusted EBIT, an entry threshold of 70% and a maximum goal achievement level of 115% were set for 2016. The goal achievement level in respect of free cash flow, on the other hand, was defined in absolute terms, with an entry threshold fixed at a figure of € 30 million below the planned level and the maximum APB entitlement at € 15 million above the target. The Supervisory Board takes each Executive Board member's individual performance into account by decreasing or increasing the APB entitlement by up to 20% (by means of the so-called discretionary factor).

Individual performance
taken into account

Performance-related components with long-term incentive effect

The Restricted Stock Plan (RSP) is awarded initially in the form of a cash settlement, subject to income tax, the full net amount of which the Executive Board member is then obliged to reinvest immediately in MTU shares. These shares must be held for a vesting period of four years.

The value of these RSP shares at the grant date represents around 60% of the variable portion of the total direct target compensation, which is weighted according to a multi-year goal achievement level. The latter is calculated by taking the arithmetical mean of the APB entitlements established for the three financial years preceding the year in which the RSP shares were granted. In the case of a new Executive Board member who has not been in office long enough to enable a multi-year goal achievement level to be established at the RSP grant date, a bonus entitlement of 100% is assumed for the missing years.

Compensation of individual members of the Executive Board

The members of the Executive Board were awarded the following total compensation – as defined in Section 314 (1) no. 6a of the German Commercial Code (HGB) – for their activities on the board in the financial years 2016 and 2015:

Compensation of individual members of the Executive Board

Executive Board member	Reiner Winkler Chief Executive Officer		Dr. Rainer Martens Chief Operating Officer	
	2016	2015	2016	2015
in €				
Non-performance-related components				
Fixed compensation	750,000	720,000	500,004	500,004
Fringe benefits ¹⁾	27,767	23,574	15,664	15,723
Performance-related components				
without long-term incentive effect (non-deferred) ²⁾	830,574	460,647	476,811	319,894
with long-term incentive effect				
Deferred APB 2013 ³⁾		162,321		146,089
Deferred APB 2014 ³⁾	309,742	343,574	205,204	227,617
Deferred APB 2015 ³⁾	354,261		246,014	
RSP 2016 ⁴⁾	1,024,974		637,146	
Share-based compensation ⁵⁾		445,295		309,263
Other ⁶⁾		231,296		155,192
Total compensation	3,297,318	2,386,707	2,080,843	1,673,782

¹⁾ Fringe benefits include charges to taxable income covering personal use of company vehicles amounting to € 63,814 (2015: € 65,098) and premiums for insurance policies taken out on behalf of members of the Executive Board amounting to € 5,407 (2015: € 5,478).

²⁾ Non-deferred APB for the financial year 2016 (or 2015); to be paid out in 2017 after adoption of the annual financial statements for 2016.

³⁾ To be paid out in 2017 after the adoption of the annual financial statements for 2016.

⁴⁾ Paid out in the current financial year after adoption of the annual financial statements for the previous year.

⁵⁾ Fair value at the grant date.

⁶⁾ Difference between cash settlement value and cumulated fair value at the grant date of the redeemed share-based payment benefits. In view of the transition to the new system of long-term compensation as of the financial year 2016, the performance shares (tranches 2013-2015) and entitlements granted under the Share Matching Plan (2010-2015) were converted into shares subject to disposal restrictions (2-year vesting period) in 2016.

⁷⁾ In the financial year 2015, Dr. Stefan Weingartner additionally received the following compensatory one-time payments: fixed compensation € 278,250, fringe benefits € 16,625, APB € 208,688 and long-term compensation € 208,688.

Michael Schreyögg Chief Program Officer		Dr. Stefan Weingartner⁷⁾ (former Executive Board member) President MTU Maintenance until March 31, 2015		Total compensation	
2016	2015	2016	2015	2016	2015
500,004	500,004		119,250	1,750,008	1,839,258
25,790	24,952		6,326	69,221	70,575
476,811	319,894		44,719	1,784,196	1,145,154
	55,128		85,627		449,165
180,037	199,702	133,414	133,414	828,397	904,307
246,014		22,360		868,649	
637,146				2,299,266	
	309,263		62,904		1,126,725
	154,082				540,570
2,065,802	1,563,025	155,774	452,240	7,599,737	6,075,754

Recommendations of the German Corporate Governance Code (GCGC)

The GCGC determines the compensation components to be disclosed individually for each Executive Board member and recommends the use of the model tables appended to the Code for this purpose. Accordingly, the following table shows the benefits granted for the financial years 2016 and 2015 as well as the minimum and maximum amounts applicable for the financial year 2016 based on the 100% goal achievement.

Benefits granted

Executive Board member	Reiner Winkler Chief Executive Officer			
	2016	2016 (Min)	2016 (Max)	2015
Individual items in €				
Fixed compensation	750,000	750,000	750,000	720,000
Fringe benefits ¹⁾	27,767	27,767	27,767	23,574
Subtotal	777,767	777,767	777,767	743,574
One-year variable compensation	540,000		1,166,400	270,000
Multi-year variable compensation	740,000		1,332,000	715,295
Deferred APB 1 (relating to 2015 and based on the old compensation system)				135,000
Deferred APB 2 (relating to 2015 and based on the old compensation system)				135,000
RSP 2016	740,000		1,332,000	
Share-based compensation				
Performance Share Plan (assessment period: 4 years)				379,752
Share Matching Plan (option period: 52 months)				65,543
Total fixed and variable compensation	2,057,767	777,767	3,276,167	1,728,869
Service cost in accordance with IAS 19	215,398	215,398	215,398	211,292
Total compensation (GCGC)	2,273,165	993,165	3,491,565	1,940,161

¹⁾ Fringe benefits include charges to taxable income covering personal use of company vehicles amounting to €63,814 (2015: €65,098) and premiums for insurance policies taken out on behalf of members of the Executive Board amounting to € 5,407 (2015: € 5,478).

Dr. Rainer Martens Chief Operating Officer				Michael Schreyögg Chief Program Officer			
2016	2016 (Min)	2016 (Max)	2015	2016	2016 (Min)	2016 (Max)	2015
500,004	500,004	500,004	500,004	500,004	500,004	500,004	500,004
15,664	15,664	15,664	15,723	25,790	25,790	25,790	24,952
515,668	515,668	515,668	515,727	525,794	525,794	525,794	524,956
310,000		669,600	187,500	310,000		669,600	187,500
460,000		828,000	496,763	460,000		828,000	496,763
			93,750				93,750
			93,750				93,750
460,000		828,000		460,000		828,000	
			263,743				263,743
			45,520				45,520
1,285,668	515,668	2,013,268	1,199,990	1,295,794	525,794	2,023,394	1,209,219
181,990	181,990	181,990	178,046	107,825	107,825	107,825	82,120
1,467,658	697,658	2,195,258	1,378,036	1,403,619	633,619	2,131,219	1,291,339

The table below, compiled in accordance with the GCGC recommendations, shows the allocation of fixed and variable compensation for the financial years 2016 and 2015 as well as the service cost (benefit expense) for the pension plan:

Allocation of compensation

	Reiner Winkler Chief Executive Officer		Dr. Rainer Martens Chief Operating Officer	
Executive Board member				
Individual items in €	2016	2015	2016	2015
Fixed compensation	750,000	720,000	500,004	500,004
Fringe benefits ¹⁾	27,767	23,574	15,664	15,723
Subtotal	777,767	743,574	515,668	515,727
One-year variable compensation	830,574	460,647	476,811	319,894
Multi-year variable compensation	3,804,690	898,693	2,739,743	727,239
Deferred APB 1 (relating to 2015 and 2014 and based on the old compensation system)	354,261	343,574	246,014	227,617
Deferred APB 2 (relating to 2014 and 2013 and based on the old compensation system)	309,742	162,321	205,204	146,089
RSP 2016	1,024,974		637,146	
Share-based compensation				
Performance Share Plan 2011-2014 ²⁾		392,798		353,533
Performance Share Plan 2012-2015	525,921		473,354	
Cash settlement for PSP, SMP	1,589,792		1,178,025	
Total fixed and variable compensation	5,413,031	2,102,914	3,732,222	1,562,860
Service cost in accordance with IAS 19	215,398	211,292	181,990	178,046
Total compensation (GCGC)	5,628,429	2,314,206	3,914,212	1,740,906

¹⁾ Fringe benefits include charges to taxable income covering personal use of company vehicles amounting to € 63,814 (2015: € 65,098) and premiums for insurance policies taken out on behalf of members of the Executive Board amounting to € 5,407 (2015: € 5,478).

²⁾ In the financial year 2015, when he ceased to be a member of the Executive Board, Dr. Stefan Weingartner was awarded a cash settlement corresponding to the total value of all performance shares granted to him in 2012-2015.

³⁾ In the financial year 2015, Dr. Stefan Weingartner additionally received the following compensatory one-time payments: fixed compensation € 278,250, fringe benefits € 16,625, APB € 208,688 and long-term compensation € 208,688.

Michael Schreyögg
Chief Program Officer

Dr. Stefan Weingartner³⁾
(former Executive Board member)
President MTU Maintenance until
March 31, 2015

2016	2015	2016	2015
500,004	500,004		119,250
25,790	24,952		6,326
525,794	524,956		125,576
476,811	319,894		44,719
1,899,394	254,830	155,774	2,273,264
246,014	199,702	22,360	133,414
180,037	55,128	133,414	85,627
637,146			
			2,054,223
836,197			
2,901,999	1,099,680	155,774	2,443,559
107,825	82,120		210,815
3,009,824	1,181,800	155,774	2,654,374

Performance-related components

Annual Performance Bonus (APB)

As of 2016, beneficiaries receive the Annual Performance Bonus in a single payment as a short-term compensation component. The performance targets set by the Supervisory Board for the 2016 Annual Performance Bonus (APB) were “adjusted EBIT” with a target of € 465.0 million (actual adjusted EBIT in 2016: € 503.0 million) and “free cash flow” with a target of € 70.0 million (actual free cash flow in 2016: € 82.0 million).

Until the financial year 2015, one half of the APB was paid as a short-term component in the calendar year following the financial year in which it was awarded. The remaining 50% of the APB was deferred and paid out in two equal portions over the following two financial years. The ultimate amount of the deferred APB depended on the goal achievement level attained in respect of the two key performance indicators at group level, and on the discretionary factor applied in the respective financial years prior to the payment.

Notwithstanding the modified APB as of the financial year 2016, the remaining deferred APB components for 2014 and 2015 will continue to run until payment is due, adjusted accordingly to the respective goal achievement level. In the case of former Executive Board member Dr. Stefan Weingartner, his deferred APB entitlement for 2013 to 2015 was based not on the goal achievement level in the respective financial year, but rather on a goal achievement level of 100% and a discretionary factor of one (1).

Restricted Stock Plan (RSP)

As of the financial year 2016, the Restricted Stock Plan (RSP) replaces the previously awarded performance-related components with long-term incentive effect, consisting of the Performance Share Plan (PSP) and the Share Matching Plan (SMP). As a transitional arrangement, active members of the Executive Board were granted a one-time cash settlement corresponding to the fair value of the granted but not-yet-exercisable tranches of PSP and SMP shares, with the obligation of immediately converting the net proceeds into MTU shares with disposal restrictions. Former Executive Board member Dr. Stefan Weingartner retains his right to 1,506 free shares at the end of the three-year vesting period for the MTU shares he purchased in 2014 under the terms of the SMP.

The multi-year goal achievement level used to weight the value of RSP shares at the grant date in 2016 is calculated by averaging the Annual Performance Bonus (APB) entitlements established for the financial years 2013, 2014 and 2015.

Rules when terminating the contracts of members of the Executive Board

The members of the Executive Board are insured under a defined benefit plan. The benefits payable to members of the Executive Board under this plan correspond to those of their peers in comparable companies.

Retirement and survivors' pensions

The members of the Executive Board earn company pension entitlements in accordance with the "MTU Pension Capital" plan, which constitutes the current post-employment benefits plan for members of the Executive Board of MTU Aero Engines AG. The goal of the plan is to provide a pension amounting to 60% of each member's basic salary after 15 years of service on the Executive Board. When this plan was introduced on January 1, 2010, the vested benefits that each member of the Executive Board had earned up until December 31, 2009 under the previous plan were transferred to the new plan in the form of initial units. This entitlement represents the benefit payable at age 60 under the old plan, adapted to reflect the ratio between the actual number of years of service with the company and the number of years from start of service with the company until age 60. The initial units transferred to the new plan correspond to the current cash value of the pension converted into a lump sum.

Once this amount had been determined, a pension account was opened for each member of the Executive Board to which further capital units are credited annually. The annual capital units are calculated on the basis of an individual contribution and an age-dependent factor, with the latter taking into account an interest rate of 6% per annum up to the age of 60. The contribution period is capped at 15 years of service on the Executive Board, or at age 60, whichever comes first. As of the age of 61, the pension account earns interest at an annual rate of 4% until such time as the pension is drawn (= bonus amount). The accrued capital units plus the units initially transferred to the account plus any bonus amounts credited to the account together make up the pension capital available to finance post-employment benefits. If a member of the Executive Board dies before reaching age 60, 50% of the benefits that he/she would otherwise have earned up to that age are added to the accrued balance on the pension account – taking into account the permissible contribution period.

Contribution period capped
at 15 years of service

As a general rule, the pension capital is paid as a single lump sum. However, at the request of the Executive Board member and with the approval of the company, the pension capital may be drawn either in ten installments (with the amassed pension capital being increased by 4% before payment of the installments) or as a lifelong pension with annual increments of 1%. In any insured event, the pension account is topped up to the level of benefits the insured party would have reached under the previous plan (guaranteed capital). Pension benefits do not become payable until such time as an insured event occurs (i.e. on reaching pensionable age, or in the event of disability or death), even if the insured party leaves the Executive Board. The pension entitlement cannot be forfeited once the initial contribution has been paid.

Reiner Winkler, Dr. Rainer Martens, and Dr. Stefan Weingartner had already been promised under the previous pension plan that their years of service with former group companies would count toward their pensions.

Details of the above-mentioned obligations and benefits are shown in the following table:

Existing post-employment benefit entitlements					
Executive Board members in €	Initial transfer amount ¹⁾	Guaranteed capital ²⁾	Annual contribution	End of contribution period	One-time payment
Reiner Winkler ³⁾	1,625,140	2,510,788	400,000	Oct. 1, 2019	7,744,205
Dr. Rainer Martens	1,366,176	2,317,650	220,000	Apr. 1, 2021	5,293,176
Michael Schreyögg	365,627	365,627	215,478	Aug. 1, 2026	4,801,945

¹⁾ Credit for past service up to December 31, 2009 (date of changeover to new system).
Michael Schreyögg: Changeover date July 1, 2013.

²⁾ Level of benefits to which the insured party would have been entitled under the previous pension plan.

³⁾ Reiner Winkler was promised a special transfer amount of € 575,065 in 2010 in connection with the changeover of his pension entitlements to the new system.

Differentiated contributions to individual pension accounts

The differences in the annual contributions to the MTU pension accounts result from the remaining periods of service on the Executive Board until the end of the respective contribution period, from the respective age-dependent factors, and from the different salary amounts eligible for pension contributions.

The following table shows the service cost for the financial years 2016 and 2015, and the corresponding carrying amounts of pension provisions recognized for members of the Executive Board in accordance with both IFRS and the German Commercial Code (HGB):

Allocations to pension provisions and total amounts recognized					
Executive Board members	Year	Service cost (IFRS)	Service cost (HGB)	Carrying amount of pension provisions at Dec. 31 (IFRS)	Carrying amount of pension provisions at Dec. 31 (HGB)
in €					
Reiner Winkler	2016	215,398	195,610	6,447,991	5,606,825
	2015	211,292	180,513	5,891,528	5,267,473
Dr. Rainer Martens	2016	181,990	168,116	4,786,287	4,220,570
	2015	178,046	156,217	4,369,536	3,943,316
Michael Schreyögg	2016	107,825	90,264	3,241,263	2,502,890
	2015	82,120	61,774	2,861,629	2,358,717
Total	2016	505,213	453,990	14,475,541	12,330,285
Total	2015	471,458	398,504	13,122,693	11,569,506

The pension obligations toward former members of the Executive Board in accordance with International Accounting Standards (DBO) amounted to € 8,039,606 (2015: € 7,167,081).

Disability pensions

Under the new pension rules of January 1, 2010, if a member of the Executive Board is disabled before reaching the age of 60, 50% of the benefits to which he/she would normally have been entitled up to the maximum age limit are added to the balance on the pension account at the time of disablement. The amount credited is based on the contributions paid in the last year of employment. This arrangement also applies if the insured party dies before reaching the age of 60.

Severance payments on premature termination of contracts for members of the Executive Boards

Under the modified terms of the Executive Board compensation system implemented as of the financial year 2016, members of the Executive Board are entitled to receive a severance payment if MTU prematurely terminates their employment contract. This severance package comprises pro-rata amounts of the board member's basic salary, APB entitlement, and long-term RSP benefits covering the period up to the date on which his/her contract would normally have expired. When calculating the amount of the severance payment, a bonus entitlement of 100% is assumed for the APB and RSP benefits that would have otherwise been awarded for the financial years within this period. The total amount of the severance payment is capped at twice the departing board member's annual target direct compensation. If the employment contract is terminated by MTU for cause, no severance package is payable. In such cases, MTU also has the right to demand repayment of the tranche of RSP shares granted in the financial year in which the contract was terminated.

Capped severance
payments

Severance payments on premature termination of contracts for members of the Executive Board in the event of a change of control or substantial changes in the ownership of MTU Aero Engines AG

In accordance with the contracts for members of the Executive Board in force as of January 1, 2016, a change of control is deemed to have occurred if, pursuant to Section 22 of the German Securities Trading Act (WpHG), a shareholder alone directly or indirectly acquires a majority of the voting rights and this results in significant disadvantages for members of the Executive Board. Significant disadvantages exist in particular if the member of the Executive Board is dismissed, his/her duties and responsibilities significantly change or if the Executive Board member is asked to agree to a reduction in salary or premature termination of their contract. In such cases, Executive Board members are accorded special rights of termination, which must be exercised within six months, with three months' notice to the end of the month. If a member of the Executive Board makes use of these special termination rights, or if the Executive Board member's contract is terminated by mutual agreement within nine months of the change of control, the board member is entitled to a severance package comprising all outstanding compensation components covering the period up to the date on which their contract would normally have expired. When calculating the amount of the severance payment, a goal achievement level of 100% is assumed for the variable compensation components. The total amount of the severance payment is capped at three times the departing board member's annual target direct compensation.