Report drafted by the Appointments and Compensation Committee of the Board of Directors of Applus Services, S.A. in relation to the proposed amendment of the Remuneration Policy of the Directors of the Company

NOTICE. This document is a translation of a duly approved Spanish-language document, and is provided for informational purposes only. In the event of any discrepancy between this translation and the text of the original Spanish-language document, the text of the original Spanish-language document shall prevail.
1. PURPOSE OF THE REPORT

In accordance with the provisions set forth in article 529 novodecies of the Spanish Companies Act, approved by Royal Legislative Decree 1/2010 of 2 July (“Real Decreto Legislativo 1/2010, de 2 de Julio, por el que se aprueba el texto refundido de la Ley de Sociedades de Capital”) (the “Spanish Companies Act”), as well as article 40.3.b) of the Regulation of the Board of Directors of the Applus Services, S.A. (“Applus” or the “Company”), the Appointments and Compensation Committee of such Board of Directors, during its meeting held on 4 May 2016, has drafted and approved this Report to justify and explain the proposed amendment to the Remuneration Policy of the Directors of the Company to be submitted to the Board of Directors, which will, in return, submit it for the approval of the General Shareholders’ Meeting of Applus.

The aforementioned proposal, whose entire text is included in the Annex attached to this Report, intends to introduce a long term incentive system for the Executive Director of the Company. The remaining terms of the Remuneration Policy of the Directors of the Company as approved by the General Shareholders’ Meeting of Applus on 18 June 2015, shall not be altered.

2. GENERAL JUSTIFICATION FOR THE PROPOSAL

As disclosed in the Initial Public Offering (IPO) Prospectus of the Company and in the directors’ remuneration annual report for years 2014 and 2015, the executive director was awarded an incentive linked to the IPO before the Applus IPO. This incentive implies the delivery of rights over shares in Applus referred to as restricted stock units, each one to be exchangeable for one Company share in accordance with a specific calendar that will end with the vesting to occur in May 2017.

This situation implies that, as from that moment onwards, the remuneration of the executive director will exclusively be composed of a fixed remuneration, a variable remuneration and a remuneration in kind, all of them on an annual basis.

As a result of the above it is important to include in the remuneration system of the executive director a long term remuneration system, linked to the creation of value for shareholders.

During the last two years the Appointments and Compensation Committee, with the support of external advisors, has been working on the design of such a system. Following a process of queries and communications with investors carried out by the Chairman of the Committee during this year 2016, there is certainty of the need to implement the system in accordance with the terms described herein. Consequently, the proposed amendment is to be submitted to the Board of Directors, which will, in return, submit it for the approval of the General Shareholders’ Meeting.
3. DETAILED EXPLANATION OF THE MAIN CHARACTERISTICS OF THE LONG TERM VARIABLE REMUNERATION SYSTEM

Amount of the variable remuneration in the long-term

Each year the long term incentive plan awards the executive director PSUs (Performance Stock Units) equal to, in principle, 60% of his fixed remuneration (even though, depending on the degree of achievement of the parameters set forth below such amount may finally fluctuate between a minimum of 0% and a maximum of 120% of his fixed remuneration), where the value of each PSU is equivalent to the average quote value of a share in the Company during the thirty days prior to the granting of the PSUs. Each PSU will be exchangeable for one Company share in accordance with the vesting schedule referred to below.

The PSUs will be granted every year immediately after the Company’s annual results are announced. If this long term incentive plan is approved by the next General Shareholders’ Meeting, the first PSUs will be granted in July 2016.

Link to Applus’ performance in the mid and long term

The PSUs awarded in each year shall be vested into shares within a three-year period as from the date day they were awarded provided that certain parameters are met, which have the purpose of ensuring that the vesting reflects the professional performance of the executive director. Provided the conditions are met, the first PSUs granted will vest in February 2019.

Link between the remuneration and Applus’ results

In particular, the vesting of PSUs will be based on the following quantitative parameters:

a) A target based on relative total shareholder return (“TSR”) accumulated within a three-year period, where the Company’s TSR will be compared with an unweighted index composed of a group of peer companies within the testing, inspection and certification industry. This parameter will represent 40% of the total PSUs granted each year.

b) A target regarding adjusted earnings per share (“EPS”) accumulated within a three-year period. This parameter will represent 60% of the total PSUs granted each year.

The system will include standard claw-back mechanisms. Likewise, the PSUs may vest early if some events occur.

4. CONCLUSION
Following the above, in accordance with the provisions set forth in article 529 novodecies of the Spanish Companies Act, the Appointments and Compensation Committee of Applus submits this proposal to the Board of Directors of the Company which shall, in return, submit it to the General Shareholders’ Meeting for its approval.

In Bellaterra, Cerdanyola del Vallès (Barcelona), 4 May 2016
Annex

Complete text of the proposed amendment

It is proposed to amend section “Remuneration of the members of the board of directors for the performance of executive duties. Variable remuneration” (without altering the other sections included in the Remuneration Policy), which shall have the following wording:

Directors’ remuneration for the performance of executive duties

Variable remuneration

Pursuant to article 27.1 of the Board of Directors’ Regulation, remuneration comprising the delivery of shares of the Company or of its group companies, share options or other share-indexed instruments, variable payments indexed to the Company’s performance or membership of pension schemes will be confined to executive directors. Deductions should be made to remuneration linked to Company earnings in line with any qualifications stated in the external auditors’ report that reduce such earnings.

The variable remuneration of the executive director comprises the following: (i) a variable annual amount in cash linked to achieving targets; and (ii) a long term incentive plan.

(i) The executive director’s variable annual remuneration in cash will be linked to achieving targets (based on the Group’s adjusted operating profit\(^1\) and operating cash flow).

The variable amount will increase by 3% for each 1% achieved in excess of the targets, up to a maximum of 250% of the variable base target (EUR 325,000). If the targets are not achieved, the variable remuneration will decrease by 10% for every 1% by which the targets are missed.

(ii) Each year the long term incentive plan awards the executive director PSUs (*Performance Stock Units*) equal to, in principle, 60% of his fixed remuneration (even though, depending on the degree of achievement of the parameters set forth below such amount may finally fluctuate between a minimum of 0% and a maximum of 120% of his fixed remuneration), where the value of each PSU is equivalent to the average quote value of a share in the Company during the thirty days prior to the granting of the PSUs. Each PSU will be exchangeable for one Company share in accordance with the vesting schedule referred to below.

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\(^1\) For this purpose, the “adjusted operating profit” will be equal to the result of subtracting the amount corresponding to the depreciation and amortization of intangible assets (excluding the goodwill depreciation) from the recurring EBITDA.
The PSUs will be granted every year immediately after the Company’s annual results are announced. In 2016, as an exception, the first PSUs will be granted in July 2016.

The PSUs awarded in each year shall be vested into shares within a three-year period as from the day they were awarded provided that certain parameters regarding total shareholder return and adjusted earnings per share, as set out below, are met. The number of PSUs that will be vested will have a value between 0% and 120% of the fixed remuneration of the executive director depending on the degree of compliance with such parameters during the three years prior to the vesting, so as to ensure that the vesting reflects the professional performance of the executive director during each three-year period. Provided the conditions are met, the first PSUs granted will vest in February 2019.

In particular, the vesting of PSUs will be based on the following quantitative parameters:

a) A target based on relative total shareholder return (“TSR”) within a three-year period, where the Company’s TSR will be compared with an unweighted index composed of a group of peer companies within the testing, inspection and certification industry.

This parameter will represent 40% of the total PSUs granted each year.

In particular, within this 40%, 50% of PSUs will be vested should the TSR performance be equal to the index and 200% of PSUs will be vested should the TSR performance be 5% greater on an annual cumulative basis than the index. Between the index and the TSR value that gives right to vest 200% of PSUs, there will be a straight line vesting between such two values. As a result, 100% of PSUs will be vested should the TSR performance be 1.67% greater than the index.

If the TSR performance is below the index, no PSUs will vest for this parameter.

b) A target regarding adjusted earnings per share (“EPS”) accumulated within a three-year period.

This parameter will represent 60% of the total PSUs granted each year.

The Board of Directors will set specific thresholds for this EPS target at which 50%, 100% and 200% (within the 60% this parameter represents) of Target PSUs will be vested. The maximum number of PSUs that will be vested will be 200% of the Target PSUs.
If the EPS performance is below the specific threshold that gives right to vest 50% PSUs, no PSUs will vest for this parameter.

If accredited inaccuracies in the data taken into account for the purpose of awarding the PSUs are observed, mechanisms will be implemented so that the Company may claim the refund of the amount corresponding to the relevant PSUs, net of any withholding, taxes or fees, effectively received by the executive director.

Likewise, the PSUs may vest early if some events occur.

The exceptional incentive referred to as the “Economic Incentive in RSUs” described in the Initial Public Offering (IPO) Prospectus of the Company, which was granted to the executive director in connection with the public offering of the Company and whose final date is 9 May 2017 will remain in force as per the terms included in such Incentive.