

# LETTER FROM THE CHAIR OF THE REMUNERATION COMMITTEE

## STM GROUP PLC

(the "Company" or "Group")  
(Incorporated and registered in the Isle of Man under number 005398V)

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### Registered Office:

STM Group PLC,  
18 Athol Street,  
Douglas,  
Isle of Man,  
IM1 1JA

13 April 2016

Dear Shareholder

### INTRODUCTION

I am writing to you on behalf of the STM Group PLC Remuneration Committee (the 'Committee'). Since taking over as Committee Chairman last year, I, along with my fellow Committee member, have been considering the Company's approach to remuneration as it enters the next phase of development. As a result, we believe that it is time to introduce a formal and complete Remuneration Policy (the "Policy").

The Policy has been constructed, in conjunction with the help of our independent advisers so as to attract, incentivise and retain those team members (main Board and senior management) who are critical to executing the business strategy.

It has been designed to deliver a suitable mix of fixed and variable compensation containing both cash and equity components linked to stretching performance targets. This should ensure that strong year-on-year performance is rewarded whilst aligning the interests of management and shareholders over the longer term.

In line with corporate governance best practice, the Company is seeking approval for a new equity based long-term incentive plan, known as the STM Group PLC Value Creation Plan (the "VCP").

This document provides the following information:

- an overview of the VCP and how it fits with other aspects of our new remuneration policy and;
- Appendix 1 of this document which provides a summary of the key terms of the VCP.

### BACKGROUND AND RATIONALE

The Company does not currently operate a long-term incentive arrangement and has applied a standalone approach to the annual bonus. The changes to both the short and long-term incentive (set out below) have been designed to ensure that:

- there is an appropriate balance between short and long-term variable pay;
- the remuneration structure is more in line with corporate governance best practice and the market construct around short and long-term incentive design;
- performance targets assess sustained corporate performance through the annual bonus and shareholder value created through the long-term incentive;
- executives remain incentivised and motivated to execute the business strategy; and
- the interests of executives are closely aligned with those of the Company's shareholders.

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## NEW REMUNERATION POLICY

There are three core aspects to the Policy as set out below:

| Element                  | Commentary   |
|--------------------------|--|
| Salary                   | <ul style="list-style-type: none"> <li>• The Committee undertook a comprehensive benchmarking exercise during 2015.</li> <li>• The majority of the necessary adjustments were made during last year and are as reflected in the relevant section of the Report and Accounts.</li> <li>• The position of Finance Director required a greater adjustment than was appropriate in one year and hence, shareholders will see a move towards this level over the course of two years.</li> </ul>  |
| Annual bonus             | <ul style="list-style-type: none"> <li>• There is currently a Group annual cash bonus scheme in place. However, the Committee wanted to consider any future scheme within the wider context of remuneration. In considering any new format the Committee also wanted to acknowledge the inherent growth potential within STM Group and as such, even threshold payments require significant EPS growth.</li> <li>• Eligibility restricted to Executive Directors.</li> <li>• Maximum annual award of 75% of salary.</li> <li>• The award will be in the form of a cash payment.</li> <li>• For any bonus payment to accrue, the Earnings Per Share prior to any exceptional items ("EPS pre exceptionals") figure achieved must be greater than the threshold target set by reference to 20% growth on prior year EPS pre exceptionals.</li> <li>• Once the threshold target has been achieved, 20% of EPS pre exceptionals in excess of the threshold target will fund the annual bonus pool for participants.</li> <li>• Once determined, the annual bonus pool will be split between the participants, in proportion to their base salary (and subject to the maximum award limit of 75% of salary).</li> <li>• Participants may choose to waive a bonus payment in any year, although they are not permitted to transfer this payment to other employees / reports.</li> </ul> |
| Long-Term Incentive Plan | <ul style="list-style-type: none"> <li>• The Group does not currently have any mechanism in place which addresses the longer term aspects of remuneration.</li> <li>• In considering any such awards, the Committee wanted to ensure that, should management continue to deliver on their growth aspirations, there is a suitable reward for those to whom it would be due.</li> <li>• Rather than consider a more traditional LTIP, the Committee has chosen to introduce a Value Creation Plan (VCP).</li> <li>• Within this, the Committee was aware of not wanting to introduce potential excessive dilution and believes that, with a maximum dilution of 5% for the plan, the proposed plan strikes that balance.</li> <li>• Further details around the VCP are given in the remainder to this letter.</li> <li>• Resolution 6 (included later in this document) is to approve the introduction of the VCP.</li> </ul>   |

# LETTER FROM THE CHAIR OF THE REMUNERATION COMMITTEE

## OVERVIEW OF THE VCP

A summary of operation of the VCP is provided below:

- Under the VCP, participants will be allocated a number of units (Performance Units) from a total pot.
- These Performance Units have no value on grant but give the participants the opportunity to share in 8.35%\* of the total value created for shareholders over the Performance Period in excess of the threshold share price (Threshold Price).
- The Threshold Price has been set at 60 pence. This is broadly equivalent to 20% p.a. share price growth over the Performance Period (10 March 2015 share price was 30.5 pence) and hence consistent with the year on year EPS pre exceptionals growth required for the annual bonus to pay-out.
- The size of the total pot at the end of the Performance Period will be determined by the Measurement Price (the 30 day average closing share price of the Company following the announcement of the 2018 financial results plus the value of any dividends paid by the Company during the Performance Period).
- The maximum number of shares that can be issued under the VCP is equal to 5% of the Company's issued ordinary share capital at the end of the Performance Period. Total dilution, under the VCP and other share plans operated by the Company will not exceed 10% over a rolling 10 year period.

*\*8.35% has been selected such that the 5% dilution cap is met once a share price of £1.50 is achieved at the Measurement Date. This would represent a fivefold increase in the Company's share price from March 2015.*

## SHAREHOLDER CONSULTATION

Whilst the Committee has not undertaken a full shareholder consultation, the proposed structure has been discussed with a number of the Company's largest shareholders who have indicated their support.

## BOARD RECOMMENDATION

The Board believes that the structure of the VCP and the other elements of the new Policy will prove effective in retaining the current management team and aligning their interests closely with those of shareholders so that they are incentivised to continue the successful execution of the business strategy and drive the creation of value for shareholders.

As a result, the Board considers the VCP along with the new Policy, to be in the best interests of the Company and shareholders as a whole, and unanimously recommends that you vote in favour of Resolution 6.

I hope that we can rely on your support at the upcoming AGM in relation to these changes. If you would like any further information about the proposed VCP structure or have any other questions in relation to the Policy, please contact me via Elizabeth Plummer, Company Secretary.

Yours faithfully,



**Jonathan Shearman**

Remuneration Committee Chairman, STM Group PLC

# SHAREHOLDER RESOLUTION

6. That the new STM Group PLC Value Creation Plan be approved.

## Appendix 1

### APPENDIX 1: SUMMARY OF THE TERMS OF THE STM GROUP PLC VALUE CREATION PLAN (“VCP”)

The following table summarises the key terms and conditions of the proposed VCP.

| Feature                          | Detail  |
|----------------------------------|---|
| Eligibility                      | <ul style="list-style-type: none"> <li>Chief Executive Officer, Chief Financial Officer and other key members of the senior management team.</li> <li>Non-Executive Directors are not eligible to participate.</li> </ul>   |
| Performance Period               | <ul style="list-style-type: none"> <li>The Performance Period commenced on 10 March 2015, the date when the Company’s 2014 results were announced, and will end one month after the Company’s 2018 results are announced.</li> </ul>  |
| Type of incentive and award type | <ul style="list-style-type: none"> <li>Participants in the VCP will be allocated a number of Performance Units from a total pot.</li> <li>At the end of the Performance Period the participant will be awarded a number of nil-cost options.</li> </ul>   |
| Summary of operation             | <ul style="list-style-type: none"> <li>Under the VCP, participants will be allocated a number of units (Performance Units) from a total pot.</li> <li>These Performance Units have no value on grant but give the participants the opportunity to share in 8.35%* of the total value created for shareholders over the Performance Period in excess of the threshold share price (Threshold Price).</li> <li>The Threshold Price has been set at 60 pence. This is broadly equivalent to 20% p.a. share price growth over the Performance Period (the 10 March 2015 share price was 30.5 pence) and hence consistent with the year on year EPS pre exceptionals growth required for the annual bonus to pay-out.</li> <li>The size of the total pot at the end of the Performance Period will be determined by the Measurement Price.</li> <li>The Measurement Price will be determined as the 30 day average closing share price of the Company following the announcement of the 2018 financial results plus the value of any dividends paid by the Company during the Performance Period. As set out below, if there is change of control during the performance period, the offer price will be used as the Measurement Price.</li> <li>Participants may choose to waive a VCP pay-out, although they are not permitted to transfer this payment to other employees / reports.</li> <li>The maximum of number of shares that can be issued under the VCP is capped at 5% of the Company’s ordinary share capital at the end of the Performance Period.</li> </ul> |
| Allocation of Performance Units  | <ul style="list-style-type: none"> <li>It proposed to allocate the Chief Executive Officer 40% of the Performance Units with the Chief Financial Officer receiving 25%.</li> <li>The Committee retains discretion to award Performance Units to Executive Directors and senior management proportionate to their value to the Company. In the case of senior management, this will be done in conjunction with the Executive Directors.</li> <li>If a new Executive Director is appointed during the performance period then the Remuneration Committee reserves the right to re-allocate the share of Performance Units at its discretion.</li> <li>The Committee will have the power to award unallocated Performance Units or to increase the percentage of the total pot held by the existing participants at the end of the Performance Period.</li> </ul>   |

Appendix 1 (continued)

| Feature                         | Detail  |          |                         |                             |     |                       |  |
|---------------------------------|---|----------|-------------------------|-----------------------------|-----|-----------------------|--|
| Conversion of Performance Units | <ul style="list-style-type: none"> <li>Awards of Performance Units will convert at the end of the Performance Period provided the Threshold Price has been achieved.</li> <li>Provided the Measurement Price is above the Threshold Price at the end of the Performance Period, a percentage of the value created is used to create a pool (Maximum Incentive Value) in line with the following table: <table border="1" data-bbox="518 481 1343 716"> <thead> <tr> <th>Scenario</th> <th>Maximum Incentive Value</th> </tr> </thead> <tbody> <tr> <td>At or below Threshold Price</td> <td>Nil</td> </tr> <tr> <td>Above Threshold Price</td> <td>Equal to 8.35% x the difference between the Measurement Price and the Threshold price x the number of shares outstanding (capped at a number of shares equal to 5% of ordinary share capital at the end of the Performance Period)</td> </tr> </tbody> </table> </li> <li>The Maximum Incentive Value, calculated in accordance with the table above will be divided by the total number of Performance Units to calculate the value of a Performance Unit.</li> <li>The aggregate value of a participant's Performance Units is calculated by multiplying the value of one Performance Unit by the number of total Performance Units subject to their award. The value is then divided by the share price (Measurement Price – excluding any dividends) on conversion to determine the number of nil-cost options over shares.</li> </ul> | Scenario | Maximum Incentive Value | At or below Threshold Price | Nil | Above Threshold Price | Equal to 8.35% x the difference between the Measurement Price and the Threshold price x the number of shares outstanding (capped at a number of shares equal to 5% of ordinary share capital at the end of the Performance Period) |
| Scenario                        | Maximum Incentive Value   |          |                         |                             |     |                       |  |
| At or below Threshold Price     | Nil   |          |                         |                             |     |                       |  |
| Above Threshold Price           | Equal to 8.35% x the difference between the Measurement Price and the Threshold price x the number of shares outstanding (capped at a number of shares equal to 5% of ordinary share capital at the end of the Performance Period)  |          |                         |                             |     |                       |  |
| Exercise of nil-cost options    | <ul style="list-style-type: none"> <li>All nil-cost options will lapse 10 years after the date of grant. The date of grant will be the date of conversion.</li> </ul>   |          |                         |                             |     |                       |  |
| Funding                         | <ul style="list-style-type: none"> <li>The Company will satisfy any shares delivered under the VCP via: <ul style="list-style-type: none"> <li><b>NEW ISSUE SHARES</b> - Note an overall limit on the number of new issue shares that can be issued under the VCP is 5% of the issued share capital at the end of the Performance Period; and / or</li> <li><b>MARKET PURCHASED SHARES</b> - the Company can alternatively settle awards by purchasing shares in the market and holding them in an Employee Benefit Trust; and / or</li> <li><b>CASH SETTLEMENT</b></li> </ul> </li> </ul>  |          |                         |                             |     |                       |  |
| Cessation of Employment         | <p><b>PERFORMANCE UNITS</b></p> <ul style="list-style-type: none"> <li>All Performance Units will lapse if a participant is a bad leaver.</li> <li>If a participant's cessation of employment is the result of specified events, for example injury, disability, ill health, retirement, redundancy or death, the Committee shall pro-rate the number of Performance Units subject to the award capable of conversion upon the proportion of the performance period completed on the date of cessation. Further, Performance Units shall only be converted if the attached performance criteria are satisfied.</li> <li>At the Committee's discretion; the Committee may determine not to pro-rate the number of Performance Units held for time.</li> </ul> <p><b>NIL-COST OPTIONS</b></p> <ul style="list-style-type: none"> <li>All nil-cost options awarded will lapse three months after cessation of employment. An additional grace period has been allowed to ensure the individual is able to exercise their options e.g. the Company may be in a close period on cessation.</li> </ul>  |          |                         |                             |     |                       |  |

Appendix 1 (continued)

| Feature   | Detail   |
|---|--|
| Change of Control                                 | <p><b>PERFORMANCE UNITS</b></p> <ul style="list-style-type: none"> <li>On a change of control, the end of the Performance Period will be deemed to be the date of the change of control. In determining the Maximum Incentive Value, the Measurement Price will be the offer price for the Company's shares.</li> <li>The Committee has the discretion to consider whether it is appropriate to adjust the number of Performance Units which convert to reflect the time elapsed from the date of grant to the occurrence of the event.</li> </ul> <p><b>NIL-COST OPTIONS</b></p> <ul style="list-style-type: none"> <li>All nil-cost options awarded will be exercisable immediately on a change of control.</li> </ul> |
| Dilution limit                                    | <p>The maximum number of shares that can be issued under the VCP is equal to 5% of the Company's issued ordinary share capital at the end of the Performance Period.</p> <p>The maximum number of shares that can be issued under the VCP and other share plans operated by the Company is equal to 10% of the Company's issued ordinary share capital over a rolling ten year period.</p>   |
| Dividends   | <p>No dividends or dividend equivalents shall be paid on accrued or vested nil cost options.</p> <p>Once nil cost options have been exercised, the Participant will receive dividends on the relevant Shares acquired in the same way as other shareholders.</p>   |
| Taxation  | <p>The vesting and exercise of nil cost options are conditional on the Participant paying any taxes due.</p>   |
| Allotment of Shares                               | <p>Shares subscribed under the VCP will not rank for dividends payable by reference to a record date falling before the date on which the Shares are acquired. Application will be made for the admission of new Shares to be issued to the Official List of the UK Listing Authority and to trading on the London Stock Exchange plc's AIM market for listed securities following the exercise of nil cost options.</p>   |
| Variation in Capital (adjustments and amendments) | <p>If there is a variation of the share capital of the Company (for example a rights issue, subdivision, consolidation, re-listing), the Committee may take this into account when determining the Maximum Incentive Value at the end of the Performance Period.</p>   |

Appendix 1 (continued)

| Feature                | Detail   |
|------------------------|--|
| Malus and Clawback     | <p>Malus and clawback provisions will apply to the VCP.</p> <p>Trigger events will be:-</p> <ul style="list-style-type: none"> <li>• discovery of a material misstatement resulting in an adjustment in the audited consolidated accounts of the Company or the audited accounts of any Group company; and/or</li> <li>• the assessment of any performance condition or target in respect of a payment was based on error, or inaccurate or misleading information; and/or</li> <li>• the discovery that any information used to determine the payment was based on error, or inaccurate or misleading information; and/or</li> <li>• action or conduct of the Participant which, in the reasonable opinion of the Committee, amounts to employee misbehaviour, fraud or gross misconduct; and/or</li> <li>• events or behaviour of the Participant have led to the censure of a Group company by a regulatory authority or have had a significant detrimental impact on the reputation of any Group company provided that the Committee is satisfied that the Participant was responsible for the censure or reputational damage and that the censure or reputational damage is attributable to him.</li> <li>• Malus will operate throughout the Performance Period.</li> <li>• The Committee believes that it will have the necessary powers under the rules of the VCP to enforce these provisions.</li> </ul> |
| General                | The Award, nil cost options, Shares acquired and any other rights granted pursuant to the VCP are non-pensionable.   |
| Non-transferability    | The Award is not transferable, except to a trustee for the Participant, in which case the trustee will be able to transfer the benefit to the participant or by Will or by the laws of descent and distribution.   |
| Amendments             | Amendments to the rules of the VCP may be made at the discretion of the Committee.   |
| Employee benefit trust | The Company will be able to fund the Employee Trust to acquire shares in the market and/or to subscribe for shares at nominal value in order to satisfy the Award granted under the VCP. Unless prior shareholder approval is obtained, the Employee Trust will not hold more than 5 per cent of the issued share capital of the Company at any one time.  |

*Note: This Appendix 1 summarises the main features of the rules of the VCP, but does not form part of them, and should not be taken as affecting the interpretation of the detailed terms and conditions constituting the rules. Copies of the rules will be available for inspection at our registered office (18 Athol Street, Douglas, Isle of Man, IM1 1JA) during usual office hours (Saturdays, Sundays and public holidays excluded). The Directors reserve the right, up to the time of the Meeting, to make such amendments and additions to the rules of the VCP as they consider necessary or desirable, provided that such amendments and additions do not conflict in any material respect with the summary set out in this Appendix 1.*