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REPORT OF THE EXECUTIVE AND SUPERVISORY  
BOARD ON CORPORATE GOVERNANCE

# CORPORATE GOVERNANCE

## Corporate Governance Report of Pfeiderer Aktiengesellschaft

### INTRODUCTION

Pfeiderer AG's Executive Board and Supervisory Board report annually on Corporate Governance at Pfeiderer AG in accordance with Clause 3.10 of the German Corporate Governance Code.

Pfeiderer AG is committed to Principles of Corporate Governance based on transparency, responsible management and control that serve to increase the Company's value. The Supervisory Board, the Executive Board, and all senior management and employees within the Pfeiderer Group are committed to this objective. The Executive Board accepts full responsibility for ensuring that the Principles of Corporate Governance are observed throughout the Group.

### THE COMPANY'S PRINCIPLES OF CORPORATE GOVERNANCE:

The principles have been published on our website and can be downloaded from there (<http://www.pfeiderer.com>).

The Supervisory Board and the Executive Board first committed Pfeiderer AG to upholding Principles of Corporate Governance in November 2002. Following this, the Company formally adopted its own Principles of Corporate Governance on January 15, 2003. Following the amendments made to the German Corporate Governance Code on June 12, 2006, the Principles of Corporate Governance which apply to Pfeiderer AG were reviewed on December 15, 2006. No amendments to the Company's Principles were necessary.

### DECLARATION OF COMPLIANCE 2006

Under Section 161 of the German Stock Corporation Act, the Executive Board and the Supervisory Board of a public listed company must issue an annual Declaration of Conformity stating to what extent they have complied, and will continue to comply, with the Recommendations of the Government Commission on the German Corporate Governance Code. In December 2006, the Executive Board and the Supervisory Board of Pfeiderer Aktiengesellschaft published the following Declaration on the Company's website:

"In 2006, Pfeiderer AG did and shall continue to comply with the binding recommendations of the Government Commission on the German Corporate Governance Code in the version adopted on June 12, 2006, with the following exceptions: Clause 4.2.3 (Compensation): The stock option plan of Pfeiderer AG adopted by resolution of the Annual Shareholders' Meeting in 2006 is not capped. No changes to the current program are envisaged."

## COMPENSATION REPORT

### Performance-related Compensation of the Executive Board

The structure of the compensation system for the Executive Board is regularly reviewed. The Working Committee of the Supervisory Board is responsible for setting pay levels for the Executive Board. Compensation received by the members of the Executive Board is based on fixed and performance-related components. The non-performance-related components include a fixed rate of compensation plus additional benefits. The performance-related components are linked directly to the Company's success, with further components acting as a long-term incentive. In particular, they involve subscription rights to Company stock awarded as part of the Company's Long-term Incentive Plan. Furthermore, members of the Executive Board and former Executive Board members have company pension entitlements. The criteria used to determine reasonable compensation levels identify the responsibilities of the relevant Board member and in keeping with the current German Stock Corporation Act his personal performance.

The fixed component of non-performance-related compensation is paid monthly in the form of a salary. Fixed compensation components of those members of the Executive Board active since 2000 (Overdiek and Ernst) were reviewed and adjusted for the first time on January 1, 2007. Members of the Executive Board also receive benefits in kind, in particular to compensate for dual housekeeping, or are entitled to use a company car. In principle, these benefits are the same for all members of the Executive Board. However, the amount of the benefit granted depends on the personal situation of each member. No loans were made to members of the Executive Board during the reporting year.

Until the end of 2006, the performance-related component of variable compensation was based on the NOPAT (net operating profit after tax) model, as well as the economic value-added indicator (EVA), and the increase of this value compared to the previous year. In addition to that, members of the Executive Board must fulfil personal targets which have a direct bearing on their levels of compensation. Depending on how the Company has developed economically and the degree to which an Executive Board member achieves his personal target, the variable components may fluctuate considerably compared to the fixed salary component. The Supervisory Board also has provided to cap variable components where unforeseen developments make this necessary. As they joined the Company at later stages of fiscal year 2006, guaranteed bonuses and performance-related bonuses were paid for Mr Noe and Dr Hopperdietzel in accordance with the scope provided under German stock corporation law.

The bonus system was changed for all members of the Executive Board as of January 1, 2007. In future, the variable components will be based on EBITDA and ROCE and in keeping with applicable German Stock Corporation Act, at the same time taking into account whether the individual members of the Executive Board have achieved their personal targets and performance levels. In 2006, the variable components as a percentage of total compensation again amounted to around 65 percent (previous year: 65 percent).

The structure of the compensation system is in line with the Recommendations of the German Corporate Governance Code.

Components in 2006	Hans H. Overdiek	Michael Ernst	Dr. Robert Hopperdietzel <sup>1)</sup>	Derrick G. Noe <sup>2)</sup>	Dr. Jürgen Koch <sup>3)</sup>
Fixed salary	■	■	■	■	■
Variable compensation:					
Group NOPAT	■	■			■
Group EVA <sup>®</sup>	■	■			■
Delta EVA <sup>®</sup> over prior-year					
Group EVA <sup>®</sup>	■	■			■
Personal targets	■	■	■	■	■

(EVA<sup>®</sup> is a registered trade mark of Stern Stewart & Co.)

<sup>1)</sup> since September 1, 2006; <sup>2)</sup> since March 15, 2006; <sup>3)</sup> until March 31, 2006

#### Compensation paid to Executive Board in 2006

In fiscal 2006, total payments received by the Executive Board (fixed salary + benefits + bonuses), including that amount paid to former member Dr Jürgen Koch who left the Executive Board on March 31, 2006, amounted to 3,993 thousand euros (2005: 2,920 thousand euros). Payments for the fiscal year include a fixed amount including benefit in kind, totalling to 1,396 thousand euros (2005: 1,116 thousand euros).

Pension commitments (provisions and current pension payments) to members of the Executive Board, former members of the Executive Board and their dependents amounted to 5,369 thousand euros (2005: 5,556 thousand euros). In fiscal 2006, no payments were made to former members of the Executive Board (2005: zero euros).

Members of the Executive Board hold a total of 284,100 Pfeleiderer shares (previous year: 430,530).

The table below shows the ratio of fixed and performance-related compensation components are shown for each member of the Executive Board:

EUROS	Fixed salary incl. benefits in kind	Performance-related	Total
Hans H. Overdiek	546,100	1,060,160	1,606,260
Michael Ernst	284,121	766,938	1,051,059
Dr. Robert Hopperdietzel (since September 1, 2006)	176,628	180,000	356,628
Derrick G. Noe (since March 15, 2006)	318,553	410,000	728,553
Dr. Jürgen Koch (until March 31, 2006)	70,352	180,000	250,352
<b>Total</b>	<b>1,395,754</b>	<b>2,597,098</b>	<b>3,992,852</b>

**STOCK OPTION PLAN**

At the Annual Shareholders' Meeting of June 13, 2006, Pfeleiderer AG's shareholders authorized a stock option plan of a maximum 4,555,330 plan shares for which stock options may be issued as part of a Pfeleiderer stock option plan. The Company decides annually, and at its own discretion, whether or not to run a stock option plan, who may take part and how many stock options participants may receive. Eligible participants are granted stock options on the condition that they make a personal investment in the Company. Stock options have a term of six years. Stock options are also subject to a three-year vesting period. The number of stock options granted to any one participant is calculated from the amount of his personal investment, divided by the strike price and then multiplied by a factor of 12 for senior management or 18 for members of the Executive Board. The strike price is calculated from the average price of the Company's share during the three months immediately prior to the expiry date of the vesting period. A quarter of the stock options held may be exercised respectively when the subscription price of at least 110, 115, 120 or 125 percent of the strike price has been reached.

Under the terms of Pfeleiderer AG's Long-term Incentive Program, members of the Executive Board are granted stock options against payment of a personal investment in the Company. In fiscal 2006, members of the Executive Board were granted a total of 233,160 options from the 2006 Stock Option Plan authorized by the Annual Shareholders' Meeting on June 13, 2006. As of balance sheet date on December 31, 2006, members of the Executive Board were entitled to 90,450 options from 2001 Stock Option Plan (SOP 2001), 69,336 options from SOP 2002, 321,884 options from SOP 2004 and 233,160 options from SOP 2006. The table below shows the stock options held by each member of the Executive Board:

Summary of stock options for members of the Executive Board:

	SOP 2001		SOP 2002		SOP 2004		SOP 2006		Total	Total	Value of
	12-31-2006	12-31-2005	12-31-2006	12-31-2005	12-31-2006	12-31-2005	12-31-2006	12-31-2006	12-31-2006	12-31-2005	options
	units	units	units	units	units	units	units	units	units	units	euros
Hans H. Overdiek	90,450	90,450	69,336	92,448	257,508	257,508	93,264	510,558	440,406		1,590,793
Michael Ernst	–	30,150	–	92,448	64,376	64,376	46,632	111,008	186,974		441,706
Dr Robert Hopperdietzel <sup>1)</sup>	–	–	–	–	–	–	46,632	46,632	–		270,466
Derrick G. Noe <sup>2)</sup>	–	–	–	–	–	–	46,632	46,632	–		270,466
Dr Jürgen Koch <sup>3)</sup>	–	60,300	–	96,300	–	64,376	–	–	220,976		0
<b>Total</b>	<b>90,450</b>	<b>180,900</b>	<b>69,336</b>	<b>281,196</b>	<b>321,884</b>	<b>386,260</b>	<b>233,160</b>	<b>714,830</b>	<b>848,356</b>		<b>2,573,430</b>

<sup>1)</sup> since September 1, 2006

<sup>2)</sup> since March 15, 2006

<sup>3)</sup> until March 31, 2006

<sup>4)</sup> The value of the options is calculated from the fair values at the time of issue of the individual SOPs.

### Compensation of the to Supervisory Board

Payment of the Supervisory Board was set by the Annual Shareholders' Meeting and is regulated in Article 15 of the Company's Articles of Incorporation. It comprises a fixed fee, an attendance fee for meetings attended and a performance-related payment. Members of the Supervisory Board are also reimbursed for expenses incurred in the course of their duties.

Each member of the Supervisory Board receives an annual fixed fee of 21,000 euros which is paid at the end of the fiscal year. When a member of the Supervisory Board attends a Supervisory Board meeting or a Committee Meeting he is entitled to an attendance fee of 750.00 euros. No payment is made for attendance at mediation meetings convened under Section 27, Subsection 3 of the German Codetermination Act. In addition, each member of the Supervisory Board may receive an annual performance-related bonus of 150.00 euros for every cent by which the dividend per share exceeds 0.11 euros as agreed by the Annual Shareholders' Meeting when distributing profits, but not exceeding the amount of the fixed fee per member of the Supervisory Board.

The normal fixed fee and the performance-related fee are doubled for the Chairman of the Supervisory Board. Every deputy to the Chairman and all chairmen of committees formed by the Supervisory Board receive 1.5 times these fees, and members of the Supervisory Board elected to committees receive 1.25 times these fees. No payment is made for membership in the mediation committee convened under Section 27, Subsection 3 of the German Codetermination Act. When a member of the Supervisory Board performs several of the above functions simultaneously, his fee is based solely on the function which carries the highest payment.

In fiscal 2006, the total compensation made to members of the Supervisory Board totalled 378 thousand euros (2005: 374 thousand euros). The payment for fiscal 2006 included fixed fees totalling 344 thousand euros (2005: 350 thousand euros). The table below shows the payments made to each member of the Supervisory Board:

EUROS	Fixed compensation: incl. attendance fee	Variable compensation	Total
Ernst-Herbert Pfeleiderer	48,750.00	4,750.00	53,500.00
Dr. Manfred Scholz	33,750.00	3,562.50	37,312.50
Wolfgang Rhode <sup>1)</sup>	37,500.00	3,562.50	41,062.50
Wolfgang Haupt	24,000.00	2,375.00	26,375.00
Frank Kratzsch <sup>1)</sup>	24,000.00	2,375.00	26,375.00
Friedhelm Päfgen	24,000.00	2,375.00	26,375.00
Rainer Stracke <sup>1)</sup>	24,000.00	2,375.00	26,375.00
Hanno C. Fiedler	32,250.00	2,968.75	35,218.75
Robert J. Koehler	24,000.00	2,375.00	26,375.00
Reinhard Hahn <sup>1)</sup>	24,000.00	2,375.00	26,375.00
Manfred Schmidt <sup>1)</sup>	24,000.00	2,375.00	26,375.00
Josef Rugge-Fechtelpeter <sup>1)</sup>	24,000.00	2,375.00	26,375.00
<b>Total</b>	<b>344,250.00</b>	<b>33,843.75</b>	<b>378,093.75</b>

<sup>1)</sup> Employees' representative

Members of the Supervisory Board hold a total of 1,812,438 shares.

### Share dealings disclosed under Section 15a of the German Securities Trading Act (“WpHG”)

Under Section 15a of the German Securities Trading Act (“WpHG”), members of the Executive Board and members of the Supervisory Board of Pfeleiderer AG, as well as certain senior executives and persons or legal entities with close personal connections to the aforementioned, must disclose their purchases and sales of shares of Pfeleiderer AG or financial instruments based thereon. In fiscal 2006, transactions have been notified to the Company and have been reported in the Corporate Governance Report as published on the Company’s website at [www.pfleiderer.com](http://www.pfleiderer.com) and duly documented in accordance with Section 10 of the German Securities Prospectus Act (“WpPG”).

#### Notification of Directors` Dealings under sec. 15a WpHG

Notification Date	Stock exchange	Issuer	Notifying Party	Transaction	Transaction volume in €
January 02, 2006	Frankfurt	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Manfred Fleischer (Head of Finance Department)	Sales of 1,605 non-parvalue shares at 16.05 €	25,760.25
January 09, 2006	Frankfurt, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Dr. Jürgen Koch (Member of the Board of Management)	Sales of 11,950 non-parvalue shares at 17.0101 €	203,270.70
January 10, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Dr. Jürgen Koch (Member of the Board of Management)	Sales of 60,300 non-parvalue shares at 17.15032 € as a result of exercising stock options for shares granted on January 09, 2006	1,034,164.30
March 29, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Sales of 385,800 subscription rights at 0.23 €	88,734.00
March 29, 2006	Stuttgart, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Sales of 26,040 subscription rights at 0.35 €	9,114.00
March 29, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Pfleiderer Unternehmensverwaltung GmbH & Co. KG (person with close relationship with a member of the supervisory board)	Sales of 500,000 subscription rights at 0.23 €	115,000.00

Notification Date	Stock exchange	Issuer	Notifying Party	Transaction	Transaction volume in €
March 30, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Pfleiderer Unternehmensverwaltung GmbH & Co. KG (person with close relationship with a member of the supervisory board)	Sales of 500,000 subscription rights at 0.48 €	240,000.00
March 31, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Pfleiderer Unternehmensverwaltung GmbH & Co. KG (person with close relationship with a member of the supervisory board)	Sales of 463,690 subscription rights at 0.50 €	231,845.00
April 03, 2006	Frankfurt, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Michael Ernst (Member of the Board of Management)	Buy of 1,500 shares (Transformation of subscription rights) at 19.30 €	28,950.00
April 03, 2006	Frankfurt, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Michael Ernst (Member of the Board of Management)	Sales of 5,836 subscription rights at 0.50 €	2,918.00
April 03, 2006	Nürnberg, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Michael Ernst (Member of the Board of Management)	Sales of 3,504 subscription rights at 0.49 €	1,716.96
April 04, 2006	Frankfurt	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Manfred Fleischer (Head of Finance Department)	Sales of 1,420 subscription rights at 0.54 €	766.80
April 07, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Pfleiderer Unternehmensverwaltung GmbH & Co. KG (person with close relationship with a member of the supervisory board)	Sales of 800,000 subscription rights at 0.71 €	568,000.00
April 11, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Wolfgang Haupt (Member of the supervisory board)	Buy of 1,250 shares (Transformation of subscription rights) at 19.30 €	24,125.00

Notification Date	Stock exchange	Issuer	Notifying Party	Transaction	Transaction volume in €
April 12, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Pfleiderer Unternehmensverwaltung GmbH & Co. KG (person with close relationship with a member of the supervisory board)	Buy of 675,921 shares (Transformation of subscription rights) at 19.30 €	13,045,275.30
April 12, 2006	off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Lombard International Assurance S.A. (legal entity with close relationship with a member of the supervisory board)	Purchase of 200,000 shares (Aquisition by exercising subscription rights) at 19.30 €	3,860,000.00
May 12, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Sales of 200,000 non-parvalue shares at 25.15 €	5,030,000.00
May 22, 2006	Frankfurt, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 1,300 shares, price per share 20.80 €	27,040.00
May 22, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 14,000 shares, price per share 20.61 €	288,540.00
May 22, 2006	Frankfurt, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 2,500 shares, price per share 21.22 €	53,050.00
May 22, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 7,000 shares, price per share 21.11 €	147,770.00
May 24, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hanno C. Fiedler (Member of the Supervisory Board)	Sales of 7,600 non-parvalue shares, price per share 20.69 €	157,244.00
June 14, 2006	Frankfurt	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 1,500 shares, price per share 17.26 €	25,890.00

Notification Date	Stock exchange	Issuer	Notifying Party	Transaction	Transaction volume in €
June 14, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 2,800 shares, price per share 17.29 €	48,412.00
June 14, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 5,500 shares, price per share 17.38 €	95,580.00
June 30, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Doris Holle-Stracke (person with close relationship with a member of the supervisory board)	Purchase of 2,250 shares, price per share 21.94 €	49,365.00
August 09, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 5,900 shares, price per share 17.20 €	101,480.00
August 25, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Jürgen Cappell (Head of Corporate Unit Accounting/ Controlling/Tax)	Purchase of 1,200 shares, price per share 16.66 €	19,992.00
August 30, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Derrick G. Noe (Member of the Board of Management)	Purchase of 820 shares, price per share 17.80 €	14,596.00
August 30, 2006	Frankfurt, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Derrick G. Noe (Member of the Board of Management)	Purchase of 2,000 shares, price per share 17.80 €	35,600.00
September 04, 2006	Neumarkt, off-exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Michael Ernst (Member of the Board of Management)	Exercising stock options comprising 30,150 shares, price per share 9.31 €	280,696.50
September 05, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Michael Ernst (Member of the Board of Management)	Sales of 10,650 non-parvalue shares, price per share 18.00 €	191,700.00
September 06, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Michael Ernst (Member of the Board of Management)	Sales of 19,500 non-parvalue shares, price per share 17.70 €	345,150.00

Notification Date	Stock exchange	Issuer	Notifying Party	Transaction	Transaction volume in €
September 15, 2006	Frankfurt, exchange	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Dr. Melanie Tuchbreiter (Head of Corporate Unit Legal Affairs)	Purchase of 262 shares, price per share 18.94 €	4,989.92
November 28, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 10,500 shares, price per share 18.95 €	198,975.00
November 28, 2006	XETRA	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	Hans H. Overdiek (Spokesman of the Board of Management)	Purchase of 4,100 shares, price per share 18.96 €	77,736.00
December 22, 2006	OTC	Pfleiderer AG Ingolstädter Str. 51 92318 Neumarkt ISIN DE0006764749	PAP Vermögens- verwaltung GmbH & Co. KG (legal entity with close relationship with a member of the supervisory board)	Sales of 180,000 shares, price per share 19.37 €	3,486,600.00