

EXPLANATORY NOTE

on the Draft Regulation on Remunerations and Compensations payable to members of the Board of Directors of Mobile TeleSystems Public Joint-Stock Company

Development of the corporate governance practices in Russia and all over the world and acceptance by the Bank of Russia in 2014 of the Corporate Governance Code (Letter of CB RF No. 06-52/2463 dated 10.04.2014) containing recommendations relating to corporate governance, including those in respect of remunerations and compensations to members of boards of directors of public companies, have become prerequisites for revision of the Regulation on Remunerations and Compensations to the members of the Board of Directors that has been in effect since 2009 (hereinafter – the Regulation).

The following key changes are proposed to be introduced in order to comply with the recommendations of the Corporate Governance Code, to improve the procedure for payment of remunerations and compensations to the members of MTS Board of Directors.

1. Changes in the Remuneration Structure

In accordance with the Code (clauses 4.2.1, 236), any forms of short-term motivation and additional financial incentives are not recommended to be applied in respect of the members of the Board of Directors. Short-term motivation covers any incentive program that provides for a performance assessment, link to the company capitalization dynamics and bonus according to the results of the period less than three years.

The effective Regulation provides for a year-end bonus as one of the remuneration elements depending on the company capitalization amount, which is a form of short-term motivation not recommended by the Code.

From this perspective, **it is proposed to waive this form of remuneration.**

The Code also prescribes to differentiate the amount of the fixed remuneration depending on the scope of the director's obligations in the company's board of directors, including as the board chairman, a board member, a chairman of the committee (clause 233).

The fixed remuneration structure provided for by the effective Regulation and consisting of the basic remuneration and that for work in the Board of Directors' Committees enables to differentiate the directors' remuneration according to the scope of their work following the Code recommendations. However, the analysis performed has revealed that the amounts, which are now provided for carrying out any additional duties, are inadequately small as compared to other elements of directors' remuneration and fail to reflect actual efforts and scopes of works related to the work in the Committees. The above amounts are also less than the amounts of remuneration for sitting on the committees in other Russian and foreign companies, which are comparable in terms of the range of activity.

Accordingly, **it is proposed to increase remunerations for working in the Board of Directors' Committees and for acting as the Chairman of the Board of Directors at the expense of the excludable bonus amounts. This will make it possible to take into account contributions to resolving the issues made by the members of the Board of Directors and by the Chairman as well as their workload.**

According to the Code, the remuneration system of members of the Board of Directors should ensure approach of financial interests of directors with long-term financial interests of shareholders, in which case “long-term holding of the company’s shares to the maximum extent facilitates approach of financial interests of members of the board of directors with long-term interests of shareholders” (clauses 4.2, 4.2.2 of the Code). Shareholding rules for directors should encourage the accumulation by them of holding and long-term ownership of shares by members of the Board of Directors, e.g. by undertaking the obligations of minimum holding period and/or minimum number of shares owned by members of the Board of Directors (clause 237 of the Code).

Taking this into consideration, it is proposed to introduce a new component of the Company’s remuneration payable to the members of the Board of Directors, that is allotment of the Company’s shares, by setting limits for disposing by a director of shares received.

Subject to the limitations suggested by the Regulation, the Directors are not recommended to dispose the received shares within the first three years of working in the Board of Directors till the value of accumulated shares is equal to the amount of annual basic remuneration. The director should remain the holder of the company’s shares for the said amount during the entire period of his activity as a member of the Board of Directors, and within one year after termination of his powers. Starting from the fourth year, the Director is free to sell his shares for the amount exceeding the amount of the annual basic remuneration, or to keep holding them. By virtue of the applicable legal requirements, the Directors are obliged to account for holding the Company’s shares and for any transactions involving such shares, therefore the Company will be able to monitor compliance with the limitations. Such information is subject to public disclosure, and violation of the limitation by a director may affect the shareholders’ decision on nominating and/or electing him for the next year.

Therefore, the proposed changes in the remuneration structure will result in:

- **excluding the annual bonus payment and appearing of a new form of remuneration as the company’s shares being made available to the director;**
- **increasing of the fixed remuneration with a focus on increase of payment for working in the committees.**

The suggested remuneration structure is in line with the practices of companies having American listing.

Comparison of the existing and suggested structure is given in the table below:

	Current Regulation	Regulation as amended
Remuneration Components	<ul style="list-style-type: none"> • Basic remuneration • Remuneration for Sitting on Committees • Year-end bonus 	<ul style="list-style-type: none"> • Basic remuneration • Remuneration for Sitting on Committees • Granting of Shares
Basic	of BoD member/ BoD Chairman – \$250,000/ \$275,000	of BoD member/ BoD Chairman – \$300,000/ \$400,000
For sitting on committees	Mandatory/other/special committee – \$15,000/ \$5,000/ \$20,000 to a member of the committee,	Mandatory/other/special committee – \$30,000/ \$25,000/ \$30,000 to a member of the committee,

	\$25,000/ \$10,000/ \$25,000 to the chairman of the committee	\$50,000/ \$30,000/ \$50,000 to the chairman of the committee
Other	Bonus – not more than \$200,000, depending on capitalization	Granting of shares – annually for the amount of \$100,000
Limit (max)	General limit – up to \$500,000 in respect of all components	Basic + committees – up to \$400,000/\$500,000 (Director/ Chairman) Shares – \$100,000

2. Other changes

The revised Regulation provides for a number of other occasional changes:

- the director entitled to receive remuneration has been defined more precisely (section I). The right for remuneration is enjoyed by all directors who are not employees (that is those not receiving payment for performing job duties) in the MTS Group of Companies and Sistema JSFC. Such approach corresponds to the foreign practice, including to that used in telecom companies (for example, in USA);
- Regulation principles have been formulated (clause 2.2 of the draft);
- it is provided that the Company may take decisions on payment of remuneration in the amounts other than those specified in the Regulation (clause 3.3 of the draft);
- a list of the grounds for reducing the remuneration amount taking into account different situations has been specified (clauses 4.3, 5.2 of the draft);
- limit of “other” (“representational”) expenses has been lowered (clause 8.1 of the draft) following the results of the practices established over the past years.