

# Report by the Supervisory Board

The Supervisory Board approved the proposal to re-open the existing € 300 million bond issued in 2005 and increase the outstanding amount from € 300 million to € 500 million.

The Board approved a proposal to the Annual General Meeting of Shareholders in March 2008 to adopt a resolution for the annual report for the financial year 2008 and subsequent years to be drawn up in English. The Board also approved the proposal to increase the dividend per ordinary share for 2007 by 20% and the proposal made to the Annual General Meeting of Shareholders regarding the final dividend to be paid out for 2007. The Supervisory Board approved the interim dividend to be paid for 2008.

As in previous years, the Supervisory Board invited managers from a number of DSM business groups and corporate staff and services departments to its meetings, to present relevant developments in their units in person. The Supervisory Board visited DSM Pharmaceutical Products' site in Linz (Austria) and was updated by local management on the business and production activities.

Discussions were held with the external auditor, Ernst & Young Accountants, about the financial statements for 2008. The Report by the Managing Board and the financial statements for 2008 were submitted to the Supervisory Board by the Managing Board, in accordance with the provisions of Article 30 of the Articles of Association, and subsequently approved by the Supervisory Board in its meeting on 17 February 2009. The financial statements were audited by Ernst & Young Accountants, who issued an unqualified opinion (see page 148 of this report). The Supervisory Board concluded that the external auditor was independent of DSM.

We submit the financial statements to the Annual General Meeting of Shareholders, and propose that the shareholders adopt them and discharge the Managing Board from all liability in respect of its managerial activities and the Supervisory Board from all liability in respect of its supervision of the Managing Board. The profit appropriation as approved by the Supervisory Board is presented on page 149 of this report.

Despite increasing economic headwinds, DSM succeeded in recording good results for 2008. The Supervisory Board wishes to express its sincere appreciation for all the efforts made by the employees and the Managing Board.

## Remuneration policy regarding the Managing Board and the Supervisory Board

This chapter comprises two parts. The first part outlines the remuneration policy as approved in 2005 and adapted in 2008 by the Annual General Meeting of Shareholders. The second part contains details of the remuneration in 2008 and expected changes in 2009.

### Remuneration policy

The objective of DSM's remuneration policy is to attract, motivate and retain the qualified and expert individuals that the company needs in order to achieve its strategic and operational objectives.

- DSM strives for a high performance in the field of sustainability and aims to maintain a good balance between economic gain, respect for people and concern for the environment in accordance with the Triple P concept (People, Planet, Profit). The remuneration policy reflects a balance between the interests of DSM's main stakeholders as well as a balance between the company's short-term and long-term strategy. In the light of the remuneration policy, the structure of the remuneration package for the Managing Board is designed to balance short-term operational performance with the long-term objective of creating sustainable value within the company, while taking account of the interests of all stakeholders.
- To ensure that highly skilled and qualified senior executives can be attracted and retained, DSM aims for a total remuneration level that is comparable to levels provided by other (predominantly Dutch) multinational companies that are similar to DSM in terms of size and complexity. For that purpose, external reference data are used.
- The remuneration policy for the members of the Managing Board is aligned with the remuneration of other senior executives of DSM.
- In designing and setting the levels of remuneration for the Managing Board, the Supervisory Board also takes into account the relevant provisions of statutory requirements, corporate governance guidelines and other best practices applicable to DSM. DSM's policy is to offer the Managing Board a total direct compensation comparable with the median of the (predominantly Dutch) labor-market peer group.

### Labor-market peer group

In order to be able to recruit the right caliber of people for the Managing Board and to secure long-term retention of the current Board members, DSM has taken external reference data into account in determining adequate salary levels. For that purpose, a specific labor-market peer group has been defined which consists of a number of Dutch and some European companies that are more or less comparable to DSM in terms of size, international scope and business portfolio.

The labor-market peer group currently consists of the following twelve companies:

Aegon	Nutreco
AkzoNobel	Océ
Ciba <sup>1</sup>	Rhodia
Clariant	Solvay
Heineken	TNT
KPN	Wolters Kluwer

<sup>1</sup> Will be eliminated from the peer group and replaced due to the expected de-listing of the company.

Professional independent remuneration experts (Towers Perrin, Amsterdam) have adapted the raw data of the peer-group companies using a statistical empirical model, so as to make them comparable with a company the size of DSM, with the associated scope and responsibilities of the Managing Board. Peer-group data are updated on an annual basis. The peer group is verified by the Supervisory Board each year based on market circumstances (mergers, acquisitions) which determine the appropriateness of the composition of the labor-market peer group.

DSM operates in a competitive international industry. Therefore, DSM will also closely monitor industry and company-specific international developments with respect to remuneration.

Below, the various remuneration components are addressed separately.

### Base salary

On joining the Board, the Managing Board members receive a base salary that is comparable with the median of the labor-market peer group. Every year base-salary levels are reviewed. Adjustment of the base salary is at the discretion of the Supervisory Board, which takes into account external and internal developments.

### Bonus

Managing Board members can earn a bonus amounting to 60% of their annual base salary for on-target performance. Under the bonus plan, the part of the bonus that is related to financial targets accounts for 42% of base salary, which can increase to 84% in the case of an exceptionally good financial performance.

The part of the bonus that is not related to financial targets accounts for 18% of the base salary and cannot increase beyond that. Targets are defined in the areas of the company's strategic development and Triple P, among other things.

#### Bonus part linked to financial targets

The part of the bonus that is linked to financial targets includes elements related to operational performance, being operating profit (EBIT), net cash and net sales growth (organic), reflecting short-term financial results.

The weighting given to the individual financial elements in the bonus is as follows: EBIT 21%, net cash 12% and net sales growth 9% of annual base salary for on-target performance.

Targets	On-target pay-out (% of base salary)	Maximum pay-out (% of base salary)
Financial targets:		
- Operating profit	21	42
- Net cash	12	24
- Net sales growth	9	18
Non-financial targets:		
- Shared	12	12
- Individual	6	6
<b>Total</b>	<b>60</b>	<b>102</b>

#### Operational performance

Three financial-target-related bonus elements can be derived from the financial statements:

- Operating profit: EBIT before exceptional items
- Net cash, defined as cash provided by operating activities
- Net sales growth, excluding currency fluctuation

Targets are determined each year by the Supervisory Board, based on historical performance, the operational and strategic outlook of the company in the short term and expectations of the company's management and stakeholders, among other things. The targets contribute to the realization of the objective of long-term value creation.

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The company does not disclose the actual targets, as they qualify as commercially sensitive information.

## Stock incentives

The Managing Board members are eligible to receive performance-related stock options and shares. Both stock options and performance shares operate on the basis of the same performance schedule.

The vesting of stock options and performance shares is conditional on the achievement after three years of previously determined target levels of total shareholder return (TSR) compared to the peer group (see also table below).

The Chairman will receive 10,000 performance shares and 37,500 performance options; the members of the Board will receive 8,000 performance shares and 30,000 performance options.

## Exercise price

The stock options and shares are granted on the first 'ex-dividend' day following the Annual General Meeting of Shareholders at which DSM's financial statements are adopted. The exercise price of the stock incentives is equal to the opening price of the share on the date of grant at Euronext Amsterdam.

## TSR as a performance measure

DSM's TSR performance is compared to the average TSR performance of a set of pre-defined peer companies.

The TSR peer group for 2008 consists of the following companies:

AkzoNobel	Lanxess
BASF	Lonza Group
Ciba <sup>1</sup>	Novozymes
Clariant	Rhodia
Danisco	Solvay
EMS Chemie Holding	

<sup>1</sup> Will be eliminated from the peer group and replaced due to the expected de-listing of the company.

The peer group used for benchmarking TSR performance reflects the relevant market in which DSM competes for shareholder preference. It includes sector-specific competitors that the Supervisory Board considers to be suitable benchmarks for DSM.

The peer group is verified by the Supervisory Board each year based on market circumstances (mergers, acquisitions) that determine the appropriateness of the composition of the performance peer group. Depending on DSM's performance compared to the peer group a certain number of options will become exercisable and a certain number of shares will be unconditionally awarded. The stock options can be kept for a maximum of eight years (including the three-year vesting period) while the shares shall be retained by the members of the Managing Board for a period of at least five years (after the three-year vesting period) or at least until termination of employment if this period is shorter. The final performance of DSM versus its peers will be determined and validated by a bank and audited by the external auditor at the end of the performance period.

## Performance incentive zone

The number of options and shares that become unconditional after three years is determined on the basis of DSM's performance relative to the average TSR performance of the peer group. The difference between DSM's performance and the peer group's performance (in percentage points) determines the vesting.

The following table gives an overview of the vesting conditions.

DSM performance minus peer-group performance in % points	Percentage of stock incentives that vest
≥ 20	100
≥ 10 and < 20	75
≥ (10) and < 10 (target)	50
≥ (20) and < (10)	25
< (20)	0

For the 2009 TSR vesting scheme see the discussion of changes expected in 2009 at the end of this chapter.

## Pensions

The members of the Managing Board are participants in the Dutch pension fund Stichting Pensioenfonds DSM Nederland (PDN). PDN operates similar pension plans for various DSM companies. The pension provision of the Managing Board is equal to the pension provision for the employees of DSM Limburg B.V. and DSM Executive Services B.V. employed in the Limburg area.

## Employment contracts

### Term of employment

The employment contracts of the members of the Managing Board appointed before 1 January 2005 have been entered into for an indefinite period of time. Newly appointed members of the Managing Board are also offered an employment contract for an indefinite period of time. The employment contract ends on the date of retirement or by notice of either party.

### Term of appointment

Members of the Managing Board appointed before 1 January 2005 are appointed for an indefinite period of time. New members of the Managing Board (appointed after 1 January 2005) will be appointed for a period of four years. Newly appointed members are subject to reappointment by the shareholders after a period of four years.

### Notice period

Termination of employment by a member of the Managing Board is subject to three months' notice. A notice period of six months will for legal reasons be applicable in the case of termination by the company.

### Severance arrangement

There are no specific contractual exit arrangements for the members of the Managing Board appointed before 1 January 2005. Should a situation arise in which a severance payment is appropriate for these Board members, the Remuneration Committee will recommend the terms and conditions. The Supervisory Board will decide upon this, taking into account usual practices for these types of situations, as well as applicable laws and corporate governance requirements.

The employment contracts of newly appointed members of the Managing Board (appointed after 1 January 2005) include an exit-arrangement provision which is in accordance with best-practice provision II.2.7 of the Dutch corporate governance code (that is, a sum equivalent to the fixed annual salary, or if this is manifestly unreasonable in the case of dismissal during the first term of office, two times the fixed annual salary).

## Remuneration policy for the Supervisory Board

The remuneration package of the Supervisory Board comprises an annual fixed fee and an annual committee-membership fee. The fixed fee for the Chairman of the Supervisory Board is € 50,000. The members of the Supervisory Board each receive a fixed fee of € 35,000. Committee membership is awarded € 5,000 per member and € 7,500 for the Chairman. Following the splitting-up of the

Nomination and Remuneration Committee into two separate committees in 2008, the membership and chairmanship fees for each of these committees were halved.

In accordance with good corporate governance, the remuneration of the Supervisory Board is not dependent on the results of the company. This implies that neither stock options nor shares are granted to Supervisory Board members by way of remuneration.

If any shareholdings in DSM are held by Supervisory Board members, they serve as a long-term investment in the company. At year-end 2008 the members of the Supervisory Board together held no shares in Royal DSM N.V.

DSM does not provide any loans to its Supervisory Board members.

## Remuneration in 2008 and changes expected in 2009

### Remuneration of Managing Board in 2008

The remuneration package for the Managing Board is subject to annual review. The market competitiveness of the remuneration package of the Managing Board for 2008 was reviewed, based on the labor-market peer group. The data reflect the July 2008 remuneration levels. All values are denominated in euros.

On-target bonus and stock-incentive grants are expressed as a percentage of base salary. The remuneration data of peer group companies are regressed to reflect the size and scope of DSM. Stock-incentive valuations are based on the Black-Scholes method.

Furthermore, data are presented as median actual levels.

### Benchmark against labor-market peer group 2008

#### Managing Board Chairman

	DSM (1 July 2008)	Peer-group median
Base salary	€ 766,000	€ 755,000
On-target bonus	60%	100%
Total cash on target	€ 1,225,600	€ 1,510,000
Annualized stock incentive value	38%	80%
Total direct compensation	€ 1,516,680	€ 2,114,000

#### Other Board members

	DSM (1 July 2008)	Peer-group median
Base salary	€ 509,000	€ 500,000
On-target bonus	60%	70%
Total cash on target	€ 814,400	€ 850,000
Annualized stock incentive value	46%	55%
Total direct compensation	€ 1,048,540	€ 1,125,000