

Compensation system for Board of Management members

In December 2020, Covestro AG's Supervisory Board resolved to revise the compensation system for Board of Management members approved by the Annual General Meeting on May 3, 2016, effective January 1, 2021. The total target compensation remains essentially the same. The changes primarily entail adding a sustainability component to long-term variable compensation, introducing rules for withholding or recovering variable compensation components (malus and clawback), and defining maximum compensation. These modifications were made pursuant to the provisions of the Act Implementing the Second Shareholders' Rights Directive (ARUG II) and the German Corporate Governance Code as amended on December 16, 2019.

The compensation system for the Board of Management members, which has been revised as described, was approved by the Annual General Meeting on April 16, 2021, with a majority of 91.66%.

Basic principles of the compensation system for the Board of Management

The system for compensating Board of Management members is aligned with the company's strategy and is structured to help Covestro achieve sustained business success and meet its strategic goals. We aim to position Covestro as an attractive employer in the competition for highly qualified executives, guarantee a high degree of transparency and, at the same time, ensure statutory and regulatory compliance.

The Board of Management's compensation mainly comprises multi-year, performance-based variable elements in addition to non-performance-related components. This overall compensation package therefore focuses on the company's sustainable and long-term business performance.

In accordance with the Board of Management's collective responsibility under our "We are 1" philosophy, the same performance indicators are applied to determine the variable compensation of all Board of Management members. Linking compensation to financial success ensures that variable compensation will rise/fall considerably if actual results come in well over/under target. Board of Management compensation is in line with the basic principles of the compensation structure and, as a principle, is structured uniformly for the Board of Management as well as for other executives, including managerial employees, in the Covestro Group.

The Supervisory Board's objective is to offer the Board of Management competitive, market-level compensation that factors in Covestro's size and complexity as well as its financial position, including in respect of competitors. The compensation system is clearly and understandably structured and documented.

Process for determining, implementing, and reviewing Board of Management compensation

Board of Management compensation is determined by the Supervisory Board in accordance with Section 87 (1) of the German Stock Corporation Act. The Human Resources Committee assists the Supervisory Board in this process by making recommendations regarding the Board of Management's compensation system that are in turn discussed and voted on by the Supervisory Board as a whole. The Supervisory Board is permitted to obtain advice from third-party compensation consultants, if necessary, and ensures their independence if they are hired.

Additionally, the Human Resources Committee conducts the groundwork for regular reviews by the Supervisory Board of the compensation system and compensation amounts for Board of Management members. If required, it recommends that the Supervisory Board make changes to the compensation system. The applicable provisions of the German Stock Corporation Act and the GCGC as well as the Rules of Procedure of the Supervisory Board on handling possible conflicts of interest in Supervisory Board activities are also followed in the process of determining, implementing, and reviewing the compensation system.

The compensation system is presented to the Annual General Meeting for approval in the event material changes are made, or otherwise no less frequently than every four years. If the Annual General Meeting does not approve the compensation system put to a vote, the compensation system must be reviewed and again presented for a resolution no later than at the following regularly scheduled Annual General Meeting. Until such a resolution on a reviewed system has been taken, the presented remuneration system shall apply.

In exceptional cases, such as a major economic crisis, the Supervisory Board can, on the recommendation of the Human Resources Committee, temporarily deviate from the components of the Board of Management's compensation system (procedure and rules regarding the compensation structure and amounts as well as the individual compensation components), if this is in the interest of preserving the company's long-term financial health.

The present compensation system for Board of Management members is applied when current Board of Management employment contracts are renewed and when new contracts are signed. In the beginning of 2021, the regulations on malus and clawback have been supplemented in the Board of Management employment contracts currently in effect in cases where these were not already included.

Determining total target compensation

The Supervisory Board determines the total target compensation for the upcoming fiscal year for each Board of Management member in accordance with the compensation system. This compensation is appropriate in view of the Board of Management member's duties and takes into account Covestro's financial situation, performance, and future prospects.

The amount of compensation awarded to Board of Management members is reviewed annually for appropriateness by the Supervisory Board. The Human Resources Committee prepares a horizontal and vertical comparison for this purpose and, in the event changes are required, drafts a proposed resolution for the Supervisory Board. As a rule, the amount of the adjustment is limited to the change in the consumer price index for Germany.

The total target compensation amount can vary from Board member to Board member. For instance, an outstanding Board of Management member may receive a higher compensation, although the compensation structure is uniformly applied.

Horizontal/external market comparison

The benchmark used to determine whether the total target compensation is aligned with market practice is the compensation of Board of Management members of all companies listed on the German DAX and MDAX stock indexes (not including banks and insurance companies due to limited comparability). Covestro is compared with these companies to determine, in particular, whether Covestro's relative position within this group in terms of revenue, number of employees, and market capitalization is in line with the relative positioning of Board of Management compensation.

Vertical/internal market comparison

In determining Board of Management compensation, the Supervisory Board also takes into consideration the compensation structure within the company. This process involves comparing the Board of Management's compensation with that of the upper management levels (senior leaders) and of Covestro's entire German workforce (employees subject to and not subject to collective bargaining agreements, including senior leaders) over time. Senior leaders are defined as executives in the two levels below the Board of Management.

Compensation structure and components

The Covestro Group's compensation structure – not including fringe benefits and pension benefits – based on average total annual compensation for a Board of Management member at 100% target attainment is currently as follows:

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|---|----------------------------|-------------|
| • Fixed annual compensation: | | approx. 30% |
| • Short-term variable compensation (STI): | 100% of fixed compensation | approx. 30% |
| • Long-term variable compensation (LTI): | 130% of fixed compensation | approx. 40% |

The ratio of LTI to STI is therefore 57:43.

The compensation system allows the Supervisory Board to change the relative weighting of the components while conducting the annual review of Board of Management compensation. The stipulated bandwidth is between 25% and 31% for short-term and between 39% and 45% for long-term variable compensation, each in relation to the total of fixed compensation and variable components (at 100% target attainment). This ensures that the long-term portion always exceeds the short-term in line with the requirements of the German Stock Corporation Act

and the recommendations of the GCGC. The variable component of Board of Management compensation is therefore largely focused on the long term. In this way, the total compensation can be composed and weighted to consider market standards and appropriateness and, for example, to more heavily focus the compensation of Board of Management members on long-term company performance.

The additional components of total target compensation include fringe benefits, which make up around 5% of fixed compensation in each case. The defined annual contribution to retirement pensions amounts to approximately 35% of fixed compensation.

In addition, the compensation system stipulates share ownership guidelines according to which Board of Management members are required to hold shares of the company for a specified period. The Supervisory Board also has the option of partly or entirely withholding variable compensation under certain circumstances, or request the return of variable compensation already paid out (malus and clawback rules). The Board of Management's compensation is supplemented with appropriate and market-standard entitlements connected with the beginning and end of Board of Management service or a change in work location.

Overview of the Compensation system for Board of Management members

Compensation component	Basis for calculation/parameters	Strategic targets
Fixed annual compensation	<ul style="list-style-type: none"> Fixed, contractually agreed compensation paid out in 12 monthly installments. Adjustment generally limited to change in consumer price index for Germany. 	The amount of fixed annual compensation is determined based on the function and responsibilities exercised and market conditions.
Fringe benefits	<ul style="list-style-type: none"> Vehicle allowance, use of the company carpool Security services Health screening examinations If applicable, signing bonuses (payment of missed variable compensation from the previous employer, reimbursement of moving costs) 	These services are intended to ensure that Board of Management members are ready and able to work.
Short-term variable compensation (STI): "Covestro PSP"	<ul style="list-style-type: none"> Target value: currently 100% of fixed compensation Performance indicators (weighted at 1/3 each): <ul style="list-style-type: none"> Growth (core volume growth) Liquidity (FOCF) Profitability (ROCE) Payout: after one year, between 0% and 250% of the target value 	The same performance criteria that are used in managing the Group are applied to short-term variable compensation, which guarantees a direct link between the company's annual performance and this compensation component.
Long-term variable compensation (LTI): "Prisma"	<ul style="list-style-type: none"> Target value: currently 130% of fixed compensation Performance indicators (multipliers, current weighting in parentheses): <ul style="list-style-type: none"> Total shareholder return (TSR factor); multiplied by <ul style="list-style-type: none"> Outperformance factor (75%): Relative share price performance compared to the STOXX Europe 600 Chemicals index CO₂ factor (25%): Reduction in GHG emissions Payout: after four years, between 0% and 200% of the target value 	The long-term variable compensation is geared toward the sustained, future-oriented, and continuous growth of the company's value and guarantees the implementation of Covestro's vision in operations.
Absolute cap on compensation	<ul style="list-style-type: none"> The maximum total compensation (including fixed compensation, fringe benefits, variable compensation components, pension benefits) amounts to €9.0 million for the Board of Management Chair and €5.5 million for the regular Board of Management members. 	Limits according to German Corporate Governance Code rules, avoidance of inappropriately large payouts
Share ownership guidelines	<ul style="list-style-type: none"> Obligation within three years of initial appointment to invest 100% of fixed annual compensation in Covestro shares and to hold them for the duration of Board of Management service 	Linking a portion of the Board of Management members' personal assets to changes in the company's value
Malus and clawback clause	<ul style="list-style-type: none"> The Supervisory Board is entitled to withhold variable compensation (malus) or request the return of variable compensation already paid out (clawback), either in whole or in part, in the event of serious misconduct or material misstatements in financial reporting. 	Upholding our principles according to which integrity determines Covestro's actions and the company acts in compliance with the law and ethical principles without exception.
Post-employment benefits	<ul style="list-style-type: none"> Defined contribution plan Covestro contribution of up to 36% of fixed compensation over the social security contribution ceiling Contribution by Board of Management member: max. 10% over the contribution ceiling Instead granting of a fixed annual payment as pension substitute (Versorgungsentgelt) possible for future Board of Management members 	Providing contributions for an adequate retirement pension
Contract termination	<ul style="list-style-type: none"> The amount of the payments – including fringe benefits – may not exceed two years' compensation according to the GCGC recommendation and may not compensate more than the remaining term of the employment contract. Exception: Termination for good cause Post-contractual noncompete agreement for no more than two years 	Avoidance of inappropriately large payments
Change of control	<ul style="list-style-type: none"> In the event of contract termination as the result of a change of control, coverage amounting to 2.5 times the fixed annual compensation The amount of the severance payments is limited to the remaining compensation up to the expiration of the employment contract and is subject to the cap defined by the GCGC. 	Avoidance of Board of Management members not acting entirely in the company's interest out of insecurity about their positions in the event of a change of control

Absolute caps and maximum total compensation

In order to reach a balanced risk-opportunity profile, the short-term and long-term variable compensation is structured so that the payout can fall to zero. Absolute caps are defined for both compensation components. These amount to 250% for short-term variable compensation and 200% for long-term variable compensation, each as a percentage of the individual target value.

Pursuant to Section 87a (1) sentence 2 No. 1 of the German Stock Corporation Act, the Supervisory Board has stipulated maximum total compensation for the Board of Management members. The absolute amount in euro for the maximum possible payout includes fixed compensation, fringe benefits (e.g., vehicle allowance, payments toward the cost of security equipment, health screening examinations, etc.), capped variable compensation components, and pension benefits. As a result, the maximum total compensation for a full fiscal year for the Chair of the Board of Management amounts to €9.0 million, while this amount for the regular Board of Management members is €5.5 million. In the event this maximum limit is exceeded, the payout of the long-term variable compensation is reduced accordingly (as the most recent component received).

Compensation design in detail

Non-performance-related components

The non-performance-related compensation comprises the fixed annual compensation, which reflects the responsibilities and performance of the Board of Management members, along with fringe benefits.

Fixed annual compensation

The level of the non-performance-related, fixed annual compensation for members of the Board of Management takes into account the functions and responsibilities assigned to them as well as market conditions. It is paid out in 12 monthly installments.

Fringe benefits

Fringe benefits mainly comprise a vehicle allowance, use of the company carpool, the availability of security services, and reimbursement of the cost of an annual health screening examination. Under certain circumstances, such as a member who lives abroad or holds non-German citizenship, reasonable costs for preparation of tax returns by an external accountant can also be reimbursed. Fringe benefits are reported at cost or the amount of the pecuniary advantage gained.

Performance-related components

The performance-related compensation comprises a short-term variable component, which depends on the attainment of the company's target profitability, and long-term variable compensation, i.e., the stock-based compensation program Prisma, to which a sustainability component was added. Prisma is linked directly to changes in Covestro's share price.

Short-term variable compensation

The target value of the short-term variable compensation (STI) is currently 100% of the fixed annual compensation. The award is based on the performance criteria of growth, liquidity, and profitability, which are used as part of Covestro's management system to plan, manage, control, and report on business performance. This means that short-term variable compensation is directly linked to the company's success. Prior to the start of the fiscal year, the Supervisory Board determines the performance indicators to be used for these criteria and the specific applicable targets.

The above-mentioned performance criteria are applied in the Group-wide short-term Covestro Profit Sharing Plan (Covestro PSP). The Covestro PSP was introduced in 2016 and is applicable to all of Covestro's employees worldwide (with a few exceptions due to stipulations in collective bargaining agreements). Currently, the members of the Board of Management participate as well in the Covestro PSP and receive their short-term variable compensation under the rules of this plan. The following performance indicators are weighted equally and used for this purpose:

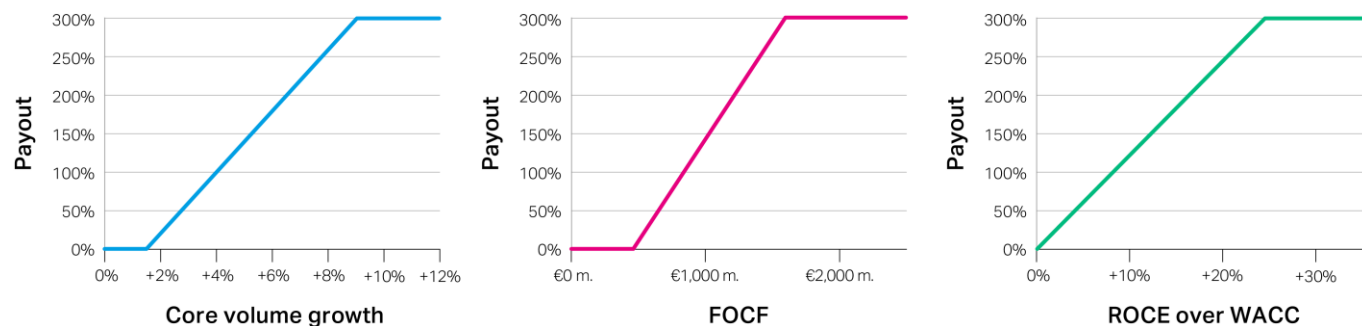
- Core volume growth
- Free operating cash flow (FOCF)
- Return on capital employed (ROCE)

The Supervisory Board defined the global values for the threshold, 100% payout and the maximum amount for each performance indicator, which are applied for a multi-year period from 2019 to 2021. Between these values, linear interpolation is used to determine the payout. There will be no adjustment after the fact. For each individual performance indicator, the payout can be between zero (failure to meet minimum requirements) and 300%. The total payout is the arithmetic mean of the individual payouts for all three components. However, it is limited to 250% of the target value corresponding to a maximum payout of 2.5 times the fixed annual compensation. This wide bandwidth ties the short-term variable compensation to the normally cyclical course of our business and ensures that profitable years result in attractive payouts, while in less profitable ones, it can be very low or even zero.

Components of the Covestro Profit Sharing Plan 2019–2021

	Growth: Core volume growth	Liquidity: FOCF	Profitability: ROCE
Threshold (0%)	+1.5%	Cash inflow of €400 million	ROCE = WACC
100% payout	+4.0%	Cash inflow of €800 million	8% points above WACC
Ceiling (300%)	+9.0%	Cash inflow of €1,600 million	24% points above WACC

Relation between payout and growth, liquidity and profitability



The Supervisory Board is entitled to reduce the STI payout to below the calculated amount or resolve to eliminate it entirely to the extent that target attainment falls far short of expectations or a major incident occurs e.g., when the Covestro Group's profitability measured as ROCE comes in below the weighted average cost of capital (WACC), or if an incident occurs at one of Covestro's plants resulting in death or a large-scale discharge of chemicals that affects the surrounding areas.

Long-term variable compensation

The target value for long-term variable compensation (LTI) currently amounts to 130% of fixed annual compensation. Participation requires that members of the Board of Management fulfill the share ownership guidelines applicable to them. The Prisma LTI plan takes into account the performance of Covestro shares, including the dividend (total shareholder return) and outperformance against the STOXX Europe 600 Chemicals industry index over a period of four years. From 2021 onward, the LTI plan also includes a sustainability component. In this form, Prisma is also applicable to Covestro executives.

A new Prisma tranche with a four-year performance period is issued for each fiscal year. At the beginning of this performance period, the Supervisory Board stipulates the performance criteria for outperformance and sustainability as well as the relative weighting of these two criteria, which are linked to the overall criterion of total shareholder return as multipliers.

The payout is determined by calculating three factors:

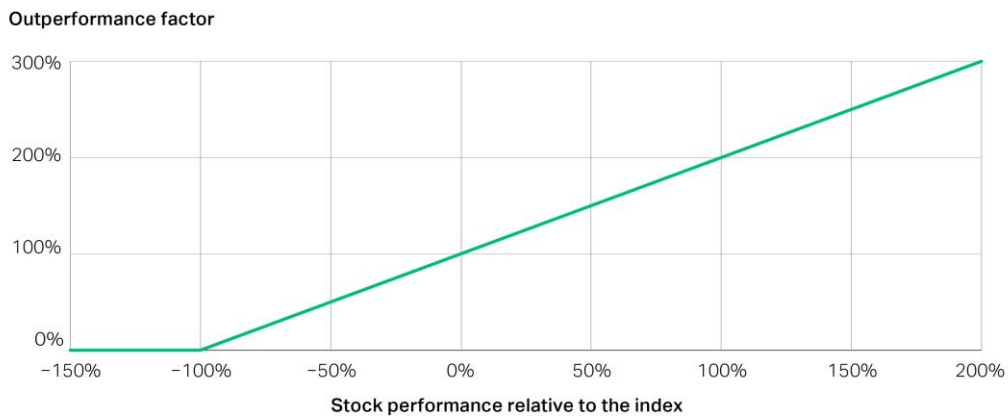
The **total shareholder return (TSR) factor** is the return generated by a stock expressed as a percentage (total of the final price of the Covestro share and all dividends distributed per share during the four-year performance period divided by the initial price).

The **outperformance factor** is based on the performance of Covestro stock during the performance period relative to the performance of the STOXX Europe 600 Chemicals index. For the tranche beginning in fiscal year 2021, the following was determined:

- The outperformance factor amounts to 100% if Covestro's stock performance (in %) matches the performance of the index (in %).
- The outperformance factor is 0% if the performance of Covestro stock (in %) underperforms the index by 100 percentage points or more.
- The outperformance factor increases in proportion with the deviation if Covestro's stock performance falls within ± 100 percentage points of the performance of the index. The same is true if it outperforms the index by more than 100 percentage points.

Due to the comparatively flat dependence of the payout on outperformance that was selected, Prisma guarantees greater stability when long-term performance targets are attained in contrast to the considerably more volatile short-term variable compensation.

Relation between the outperformance factor and Covestro's stock performance

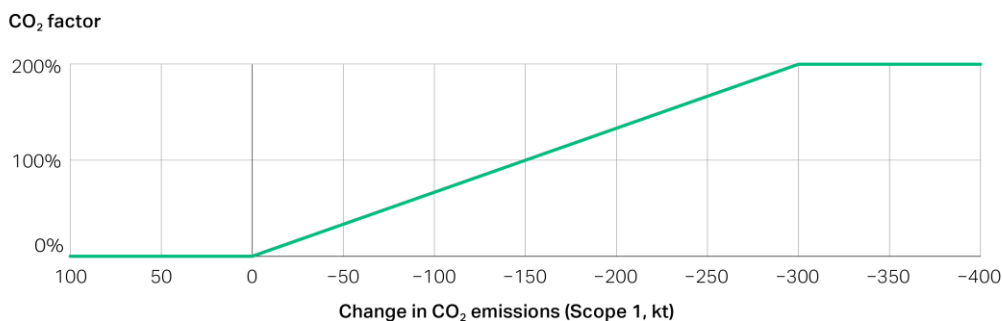


Relation between the outperformance factor and Covestro's stock performance

Stock performance relative to the index	Outperformance factor
-100% or less	0%
0%	100%
100%	200%

Starting with the tranche issued in fiscal 2021, the sustainability component applied is a reduction target for GHG emissions (CO₂ equivalents, CO₂e) classified in Scope 1. The **CO₂ factor** amounts to 100% if these emissions are reduced by 150 kilotons per year by the end of 2024 in relation to the baseline year of 2020. If the annual emissions remain unchanged, the CO₂ factor is 0%. Starting with a reduction of 300 kilotons, it reaches the maximum value of 200%. Between these values, linear interpolation is used to determine the factor. The Supervisory Board considers the defined reduction targets as significant in relation to the company's actual Scope 1 GHG emissions. Moreover, the Supervisory Board views the reduction in GHG emissions to be a relevant performance indicator to ensure the alignment of the Covestro Group's operations with the vision of fully focusing on the circular economy.

Relation between emissions and CO₂ factor



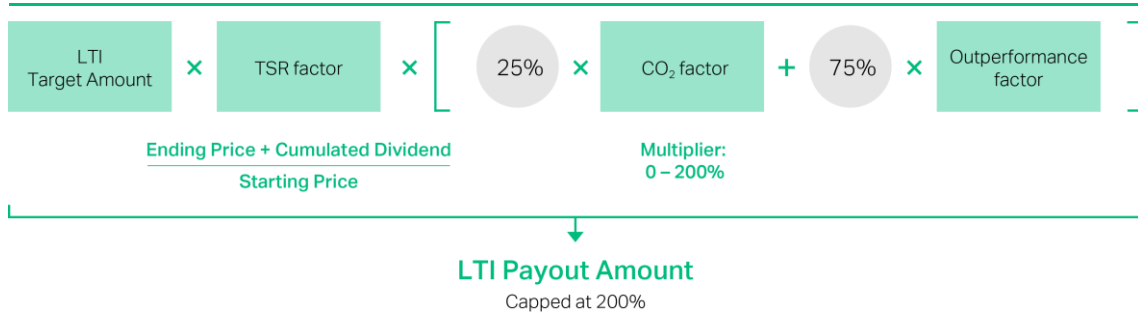
Relation between emissions and CO₂ factor

Change in annual CO ₂ emissions (scope 1) until end of 2024 compared to base year 2020	Payout
0	0%
-150 kt	100%
-300 kt	200%

In order to calculate the total payout for the tranche beginning in fiscal 2021, the LTI target opportunity is multiplied by the TSR factor, the outperformance factor weighted at 75%, and the CO₂ factor weighted at 25%. The total distribution is limited to no more than 200% of the target opportunity. The maximum payout is therefore 260% of the fixed annual compensation.

For future tranches, we plan to expand the emission reduction target to Scope 2 and Scope 3 emissions. The Supervisory Board can additionally supplement the sustainability component with additional ESG (environmental, social, governance) criteria within the framework of the existing compensation system.

Components of the long-term variable compensation



Post-employment benefits

The company pension plan in place to date (defined contribution pension commitment through Rheinische Pensionskasse) will generally continue for members of the Board of Management currently serving.

In the course of updating the compensation system, the Supervisory Board resolved to redesign Covestro's pension plan for future members. They will be granted a direct commitment to a defined-contribution company pension plan comprising retirement, disability, and survivors' benefits. For the duration of their Board of Management service, Covestro and the Board of Management members will each contribute 3% of their fixed annual compensation up to the social security contribution ceiling to a statutory pension plan. For the portion of compensation exceeding the contribution ceiling, Covestro will provide a basic contribution of 6% and a match of up to 30%, three times the Board of Management member's own contribution of no more than 10%.

This commitment is structured as a defined contribution plan. The contributions are paid into a retirement account and are guaranteed upon occurrence of the event that triggers the benefits. If a greater return is achieved prior to that time, these are credited to the retirement account at the time the beneficiary becomes eligible for benefits.

The benefits will be paid out as a lump sum or in five or ten annual payments no earlier than when the member reaches the age of 62 and leaves Covestro. In the event of disability or death, the missed contributions up to the age of 57 will be credited to the pension account.

Serving Board of Management members are free to switch their company pension to the new system as of April 2021. The Supervisory Board continues to monitor market developments and can decide within the framework of the existing compensation system to grant future Board of Management members a fixed annual payment as pension substitute instead of the pension model described here.

Share ownership guidelines

The members of the Board of Management are contractually obligated to acquire Covestro shares equivalent to 100% of the fixed compensation on their own account within three years of their initial appointment and to hold these shares for the duration of their service on the Board of Management. If their contracts are extended, this obligation is increased to the amount of the new fixed compensation. The Board of Management member in question must acquire Covestro shares equivalent to the difference within four years of starting the new period of service. The Board of Management member's individual stock holding is disclosed in the Compensation Report.

Special payments/bonuses

The Supervisory Board of Covestro AG is not authorized to grant any special payments for outstanding service at its discretion ("Mannesmann clause").

Malus and clawback clause

According to the newly introduced malus and clawback rules, the Supervisory Board can withhold short-term and/or long-term variable compensation or request the return of variable compensation already paid out, either in whole or in part, at its discretion in the event of serious breaches of duty or compliance violations. Moreover, this compensation can be clawed back if it was calculated and paid out erroneously based on incorrect data.

Any claims for repayment by the company and any right of the company to declare the forfeiture of LTI tranches not yet paid out exist even if the Board of Management member's term of service has ended at the time the claim for repayment is asserted or the declaration of forfeiture is made. The limitation period for these claims or the exercise of this right is three years. It shall begin at the end of the year in which the respective claim or right arose and the company became aware of the facts giving rise to the claim or right or should have become aware without gross negligence. Irrespective of their origin and the company's knowledge or grossly negligent lack of knowledge, such claims or such right shall lapse ten years from the relevant conduct of the Board of Management member. Other claims in the event of personal misconduct by a Board of Management member, particularly claims for damages under Section 93 of the German Stock Corporation Act, remain unaffected by the preceding.

Contract terms and benefits associated with ending Board of Management service

The Supervisory Board adheres to a maximum of five years for the term of employment contracts with Board of Management members. When they are first appointed, this should generally not be for more than three years.

If the term of Board of Management service is terminated early without good cause, the company fulfills its commitments up to the time the member leaves the company. In this case, payments to the Board of Management member, including fringe benefits, may not exceed two times annual compensation and may not compensate more than the remaining term of the employment contract (severance cap). Outstanding variable compensation components are paid out at the originally agreed times and conditions, i.e., they are not paid out in advance.

Post-contractual noncompete agreements

Post-contractual noncompete agreements exist with the members of the Board of Management, providing for compensatory payments to be made by the company for the duration of these agreements (maximum of two years). The compensatory payment amounts to 100% of the average fixed compensation in the 12 months preceding termination of service and is offset against any severance payment.

The company is entitled to waive the post-contractual noncompete agreement upon contract expiration. In this case, no compensatory payment would be made.

Change of control

In the event of a change of control that results in a material change of status of an individual Board of Management member – e.g., change in company strategy or change in the Board of Management's job responsibilities – the Board of Management member has the right to terminate the employment contract within 12 months after the change of control. When this right of termination is exercised or if the employment relationship is ended by mutual agreement on the company's initiative within 12 months of the change of control, the Board of Management member is entitled to payment of severance of 2.5 times the fixed annual compensation. The amount of the severance payments, including fringe benefits, is limited to the remaining compensation up to the expiration of the employment contract and is subject to the severance cap.

Commitments associated with starting Board of Management service or changing work location

When members of the Board of Management are initially appointed, compensatory payments may be granted for variable compensation awarded by former employers, but forfeited as a result of taking a position with Covestro. The amount of such payments is limited to the payouts due from the previous employer and include a clawback clause in the event of early contract termination.

If the appointment of a member to the Board of Management or change in work location on the initiative of the company requires a change of residence, moving costs are reimbursed up to an appropriate maximum amount determined in each contract individually.

Supervisory Board compensation

If Board of Management members hold Supervisory Board positions within the Group, the compensation for this activity is offset against fixed compensation.

They are only permitted to take external positions on other companies' Supervisory Boards with the prior consent of Covestro's Supervisory Board. In this case, the Supervisory Board decides at its discretion in each individual case whether and to what extent the compensation will be offset. A particular consideration is the extent to which the position is in the interest of the company or that of the Board of Management member.

Other information

The company holds insurance policies structured as group plans with coverage for accidents (including disability and death coverage) and for travel luggage as well as directors and officers (D&O) insurance for members of the governing bodies of the Covestro Group. In accordance with the current requirements of the German Stock Corporation Act, members of the Board of Management are subject to paying a deductible of 10% per claim. Within a fiscal year, this amount may not exceed 1.5 times the fixed annual compensation.

The company does not grant Board of Management members any loans or advances.