



## Corporate Governance Report

As a Dutch public limited liability company whose Global Depositary Receipts are listed on the London Stock Exchange, X5 Retail Group N.V. is obliged to report on compliance with the Dutch Corporate Governance Code in its Annual Report and to explain any instances where it does not apply the principles or best practice provisions of the Code.

In accordance with the Code, a broad outline of the corporate governance structure of the Company is presented in this section, including any deviations from the Code's principles and best practice provisions. The Company adheres to the principles and best practice provisions of the Code as far as may be reasonably expected, while complying with local legislation and applying market practices in the countries in which the Company operates.

### The Management and Supervisory Boards

X5 Retail Group N.V. adopted a two-tier corporate governance structure, comprising a Management Board and a Supervisory Board. Both the Management Board and the Supervisory Board are accountable to the General Meeting of Shareholders for the performance of their duties.

#### Duties of the Management Board

The Management Board is responsible for X5's overall management. It is accountable for the Company's pursuit and achievement

of corporate goals and objectives, its strategies and policies. The Management Board is responsible for complying with all relevant legislation and regulations, for managing the risks associated with the Company's activities, for financing and external communication. The Management Board is required to report related developments to, and discusses the internal risk management and control systems with the Supervisory Board and its Audit Committee.

#### Members of the Management Board

The Management Board consists of three members, the CEO, the CFO and the Company Secretary. Since the third quarter of 2010 the composition of the Management Board changed. On 29 September 2010 Mr. Evgeny Kornilov resigned as CFO of the Company. His successor, Mr. Kieran Balfe, was appointed by the General Meeting of Shareholders on 22 February 2011. Furthermore, on 10 March 2011 Mr. Lev Khasis resigned as CEO of the Company. The Supervisory Board nominated Mr. Andrei Gusev as his successor, to be appointed by the upcoming Annual General Meeting of Shareholders in June 2011. Finally, the Supervisory Board proposes to the General Meeting of Shareholders the re-appointment of Mr. Frank Lhoëst, whose first term of appointment comes to an end in 2011.

The table below shows the members of X5's Management Board and their respective terms of appointment:

Name	Year of Birth	Position	Year of Initial Appointment	End of Current Term of Appointment
Mr. Andrei Gusev <sup>(1)</sup>	1972	Chief Executive Officer, Chairman of Management Board (appointment pending <sup>(1)</sup> )	2011	2015
Mr. Kieran Balfe	1969	Chief Financial Officer	2011	2015
Mr. Frank Lhoëst <sup>(2)</sup>	1962	Company Secretary	2007	2011

<sup>(1)</sup> The Supervisory Board nominated Mr. Andrei Gusev as member of the Management Board and CEO, to be appointed by the upcoming 2011 Annual General Meeting of Shareholders.

<sup>(2)</sup> Mr. Frank Lhoëst's first term of appointment comes to an end in 2011. He is nominated by the Supervisory Board for re-appointment.



**Andrei Gusev**, a Russian citizen, joined X5 in 2006 as M&A and Business Development Director. Prior to joining X5 Mr. Gusev worked in Alfa Group as Director for Investment Planning and Director for Group Portfolio Management and Control since 2001. Mr. Gusev was leading the merger process that led to the creation of X5 Retail Group. Prior to joining Alfa Group, Mr. Gusev worked many years in strategic consulting at Bain & Company and at Deloitte & Touche. Mr. Gusev graduated with honors from the Moscow State University, and holds an MBA degree from the Wharton School of Business at the University of Pennsylvania.

**Kieran Balfe**, an Irish citizen, was appointed Chief Financial Officer of X5 on 22 February 2011. Mr. Balfe has been working in Russia since 1994. Prior to his appointment at X5 Mr. Balfe was Deputy General Manager and CFO for Emerging Markets of the confectionary leader Wrigley. Following the acquisition of Wrigley by Mars Inc., Mr. Balfe played a key role in the integration of the two companies' Russian operations.

Previously, Mr. Balfe was Financial Controller at Japan Tobacco International, Deputy General Manager and Finance Director at American Home Products Corporation responsible for both operational and corporate finance for Russia and the CIS countries, and Finance Director for Glencore's copper operations in Kazakhstan. Mr. Balfe started his career as an Audit Supervisor and Audit Manager for Coopers & Lybrand, with whom he initially relocated to Moscow in 1994. Mr. Balfe graduated from the University College Dublin with a Master's degree in accountancy. He qualified as a Chartered Accountant in 1993 and was awarded a fellowship in the Institute of Chartered Accountants in Ireland in 2005.

**Frank Lhoëst**, a Dutch citizen, was appointed as statutory director and Company Secretary of X5 on 5 November 2007. Since 1991, Mr. Lhoëst has held several positions at Intertrust Group,

from account manager in the Netherlands Antilles to founder and director of the Intertrust office in Vienna, Austria. In 2002, Mr. Lhoëst established the Intellectual Property Group of Intertrust in the Netherlands. Mr. Lhoëst graduated from the Leiden University with a degree in Law.

### **Duties of the Supervisory Board**

The Supervisory Board is responsible for advising and supervising the Management Board and the general course of affairs of X5 and its businesses. In performing its duties, the Supervisory Board takes into account the relevant interests of the Company's stakeholders, and, to that end, considers all appropriate interests associated with the Company. Major business decisions require the approval of the Supervisory Board. The Supervisory Board also supervises the structure and management of internal control systems as well as the financial reporting process. The Supervisory Board meets at least four times per year.

### **Members of the Supervisory Board**

The General Meeting of Shareholders determines the number of members of the Supervisory Board. The Supervisory Board currently consists of seven members.

The Supervisory Board has prepared a profile of its size and composition, taking account of the nature of the Company's business and its activities and the desired expertise and background of the members of the Supervisory Board. The Supervisory Board generally aims for a diverse composition, but diversity is not a decisive factor when finding the most suitable candidate in line with the Supervisory Board profile. The Supervisory Board evaluates the profile annually.

According to the Rules governing the Principles and Practices of the Supervisory Board, a person may be appointed to the Supervisory Board for a maximum of three terms of four years.



The Supervisory Board has prepared a Retirement and Re-appointment Schedule to prevent, to the greatest extent possible, re-appointments occurring simultaneously. Both the Supervisory Board profile and rotation plan can be viewed on the Company's website.

The table below shows the current members of the Supervisory Board and their respective terms of appointment.

**Hervé Defforey**, a French citizen, is an operating partner in GRP Partners, Los Angeles, and sits on the boards of IFCO Systems N.V., Ulta Corp., Chicago and Kyriba S.A., Paris. Prior to joining GRP in 2001, Mr. Defforey was CFO and Managing Director of Carrefour S.A., from 1993 to 2001, where he remained on the board until 2004. Previously, Mr. Defforey was Treasurer at BMW Group and General Manager of various BMW AG group subsidiaries, and also held senior positions at Chase Manhattan Bank, EBRO Agricolos, S.A. and Nestlé S.A. Mr. Defforey graduated from the University of St. Gallen, Switzerland with a degree in Business Administration.

**Mikhail Fridman**, a Russian citizen, serves as Chairman of the Supervisory Board of Alfa Group and is one of Alfa Group's principal founders. He also serves as the Chairman of the Board of Directors of Alfa Finance Holdings S.A. and of TNK-BP and is a member of the Board of Directors of ABH Holdings S.A. (holding company for Alfa-Banking Group) and of VimpelCom. He is also a member of the International Advisory Board of the Council of Foreign Relations (USA). Mr. Fridman graduated from the Moscow Institute of Steel and Alloys.

**David Gould**, a U.S. citizen, has been serving as Deputy Director for Corporate Development, Finance and Control at Alfa Group Consortium since 2000. He also serves as a member of the Board of Directors of Alfa Finance Holdings S.A. and of ABH Holdings S.A. (holding company for Alfa-Banking Group). From 1992 to 2000, Mr. Gould held various positions at PricewaterhouseCoopers in Boston and in Moscow. He received his BA with honours from Colgate University in 1991 (concentration in Liberal Arts and minor concentration in Economics) and received his MBA-MS (Accounting) from Northeastern University in 1992. He qualified as a Certified Public Accountant in 1993 and as a Chartered Financial Analyst in 1999.

Name	Year of Birth	Position	Year of Initial Appointment	End of Current Term of Appointment
Mr. Hervé Defforey	1950	Chairman	2006	2014
Mr. Mikhail Fridman	1964	Member	2006	2013
Mr. David Gould	1969	Member	2006	2014
Mr. Vladimir Ashurkov	1972	Member	2006	2012
Mr. Alexander Tynkovan	1967	Member	2008	2012
Mr. Stephan DuCharme	1964	Member	2008	2012
Mr. Christian Couvreur	1950	Member	2010	2014



**Vladimir Ashurkov**, a Russian citizen, serves as Director of Group Portfolio Management and Control in Alfa Group. His main non-executive/ancillary positions include member of the Supervisory Board of Alfa Group, member of the Advisory Committee of Rosvodokanal, member of the Altime Advisory Committee and member of the A1 Group Advisory Committee. Prior to joining Alfa Group, Mr. Ashurkov served as Vice President of Strategic Development in Industrial Investors Group (which owns the controlling stake in Far East Shipping Company) and gained experience in other transport and logistics companies and investment banks. Mr. Ashurkov graduated from the Moscow Institute of Physics and Technology with a Bachelor of Science (Physics) and from the Wharton School, University of Pennsylvania, with an MBA.

**Alexander Tynkovan**, a Russian citizen, is the founder and CEO of "M.Video", a leading consumer electronics and home appliance retailer in the Russian Federation. Mr. Tynkovan graduated summa cum laude from the Moscow Energy Institute, majoring in Aircraft Electric Equipment.

**Stephan DuCharme**, a U.S. citizen, currently holds a portfolio of positions, including as member of the Investment Committee of Alfa Private Equity Partners, a Russian private equity fund. Previously, he held positions with SUN Group, Alfa Group, European Bank for Reconstruction and Development (EBRD) and Salomon Brothers Inc. Mr. DuCharme has served on the Boards of Directors of CSA Czech Airlines, Alfa Bank, SUN-Interbrew Ltd. and JSC SUEK. He graduated with distinction from the University of California at Berkeley and received his MBA from INSEAD.

**Christian Couvreur**, a French citizen, currently acts as a retail consultant in Asia, in particular, in Thailand, Vietnam, Indonesia and the Philippines. He formerly held several leadership positions at Group Casino, including the position of CEO from 1997 until

2003, as well as at CFAO (now part of PPR), in particular, of CFAO-Congo and La Ruche Meridionale. Mr. Couvreur holds a Master's degree in Economic Sciences from the University of Paris and an MBA from the French business school H.E.C.

### **Committees of the Supervisory Board**

While retaining overall responsibility, the Supervisory Board assigns certain tasks to its four permanent committees: the Audit Committee, the Nomination and Remuneration Committee, the Related Party Committee and the Strategy Committee. Each committee is composed of at least two members, at least one of whom must be independent within the meaning of the Dutch Corporate Governance Code. The members of each committee are appointed by and from the Supervisory Board. The committees operate pursuant to terms of reference established by the Supervisory Board, in accordance with the Dutch Corporate Governance Code. The terms of reference of these committees can be viewed on X5's website.

**Audit Committee.** The Audit Committee assists the Supervisory Board in fulfilling its supervision and monitoring responsibilities in respect of the integrity of X5's financial statements, system of internal business control and risk management, financing and finance related strategies and tax planning. It furthermore advises in respect of the appointment of the external auditor by the General Meeting of Shareholders and his remuneration.

**Nomination and Remuneration Committee.** The Nomination and Remuneration Committee recommends the remuneration policy for the Management Board to be adopted by the General Meeting of Shareholders, prepares proposals to the Supervisory Board for remuneration of the individual members of the Management Board in line with the remuneration policy and advises the Management Board on the level and structure of compensation for other senior personnel. The Nomination and Remuneration Committee also advises in respect of the selection and appointment of



members of the Supervisory Board and the Management Board. At least annually the Nomination and Remuneration Committee evaluates the size and composition of the Supervisory Board and the Management Board, as well as the functioning of the individual members, and reports the results of such evaluations to the Supervisory Board.

**Related Party Committee.** The Related Party Committee advises the Supervisory Board on handling and deciding on reported (potential) conflicts of interests and any other related party

transactions which are contemplated between X5, on the one hand, and conflicted persons or entities, including but not limited to its shareholders, members of the Supervisory Board and members of the Management Board, on the other hand.

**Strategy Committee.** The Strategy Committee advises in respect of the general strategy of X5, including, but not limited to, the future direction to be taken by X5 as a whole and each of its affiliated businesses, overall growth and development strategy, mergers and acquisitions and financing strategy.

**Composition of the Supervisory Board Committees**

Name	Audit Committee	Nomination & Remuneration Committee	Related Party Committee	Strategy Committee
Mr. Hervé Defforey	Member	Member		Member
Mr. Mikhail Fridman				
Mr. Vladimir Ashurkov	Member	Member		Member
Mr. David Gould	Chairman			
Mr. Alexander Tynkovan		Member	Chairman	Member
Mr. Stephan DuCharme		Chairman	Member	
Mr. Christian Couvreur				Chairman

**Appointment, Suspension and Dismissal**

The General Meeting of Shareholders shall appoint the members of the Management and Supervisory Board from a list of nominees, containing names of at least two persons for each vacancy, to be drawn by the Supervisory Board. The nomination by the Supervisory Board of the candidates is binding, and therefore the recommended candidate will be appointed by the General Meeting of Shareholders unless the nomination is deprived of its binding character by a qualified majority vote of at least two-thirds of the votes cast, representing more than one-half of the issued share capital of the Company. If the recommended

candidate is rejected, the second nominee will be appointed unless similarly rejected by the General Meeting of Shareholders.

Supervisory Board members are appointed for a period of up to four years and may be re-elected twice. Members of the Management Board are also elected for a period of four years. The Articles of Association do not limit the total term of office for Management Board members.

Each member of the Supervisory Board and Management Board may, at any time, be dismissed or suspended by the General



Meeting of Shareholders. A member of the Management Board may at any time be suspended by the Supervisory Board. Such suspension may be discontinued by the General Meeting of Shareholders at any time.

### **Remuneration**

The remuneration of the individual members of the Management Board will be decided by the Supervisory Board on the recommendation by the Nomination and Remuneration Committee of the Supervisory Board, based on the Company's Remuneration Policy. The remuneration of the members of the Supervisory Board is determined by the General Meeting of Shareholders.

The Remuneration Policy for members of the Management Board and Supervisory Board is incorporated in the Remuneration Report on page 75, and is available on the website of the Company.

### **Reporting on Conflicts of Interest**

The Supervisory Board is responsible for deciding how to resolve conflicts of interest between members of the Management Board, members of the Supervisory Board and/or the external auditor on the one hand and the Company on the other hand.

A member of the Management Board or of the Supervisory Board is required to immediately report and provide all relevant information to the Chairman of the Supervisory Board (and to the other members of the Management Board, if it concerns a member of that board) on any conflict of interest, or potential conflict of interest, that he may have with the Company and that may be of material significance to him or the Company.

A decision of X5 to enter into a transaction involving a conflict of interest with a member of the Management Board or a member

of the Supervisory Board that is of material significance to him or the Company requires the approval of the Supervisory Board and must be concluded on terms customary in the Russian retail sector. The Related Party Committee advises the Supervisory Board on the handling, and deciding on, reported conflicts of interest and prepares resolutions of the Supervisory Board in relation thereto.

In the event of legal proceedings between the Company and a member of the Management Board, the Company may be represented by a member of the Supervisory Board. In all other events in which a member of the Management Board has a conflict of interest with the Company, the Company may be represented by the Management Board, notwithstanding the discretionary power of the General Meeting of Shareholders to designate other person(s) to represent the Company upon execution of such a related party transaction.

## **Shareholders and Their Rights**

### **General Meeting of Shareholders**

X5 Retail Group N.V. is required to hold a General Meeting of Shareholders within six months after the end of the financial year, among other things, to adopt the financial statements, to decide on any proposal concerning profit allocation and to discharge the members of the Management Board and Supervisory Board from their responsibility for the performance of their respective duties for the previous financial year.

Extraordinary meetings will be held as often as the Management Board or the Supervisory Board deems necessary. In addition, shareholders and holders of Global Depositary Receipts (GDRs) jointly representing 10% of the outstanding share capital may request the Management Board and the Supervisory Board that a General Meeting of Shareholders be held, stating their proposed agenda in detail.



The powers of the General Meeting of Shareholders are defined in the Articles of Association. Apart from the decisions taken at the Annual General Meeting of Shareholders, the main powers of the shareholders are to appoint (subject to the Supervisory Board's right of making binding nominations), suspend and dismiss members of the Management Board and Supervisory Board, to appoint the external auditor, to adopt amendments to the Articles of Association, to issue shares and grant subscriptions for shares, to authorise the Management Board or the Supervisory Board to issue shares and grant subscriptions for shares, to authorise the Management Board or the Supervisory Board to restrict or exclude pre-emptive rights of shareholders upon issuance of shares, to authorise the Management Board to repurchase outstanding shares of the Company, to adopt the remuneration policy of the Management Board, to determine the remuneration of members of the Supervisory Board, and to merge, demerge or dissolve the Company.

General Meetings of Shareholders may only be held in Amsterdam, Haarlemmermeer (Schiphol Airport) or The Hague (the Netherlands). The notice for a General Meeting of Shareholders needs to be published not later than the 42nd day prior to the day of the meeting. The mandatory record date, establishing which shareholders are entitled to attend and vote at the General Meeting of Shareholders, is fixed at the 28th day prior to the date of the meeting.

One or more shareholders or holders of GDRs representing at least 1% of X5's issued share capital or representing a value of EUR 50 million are entitled to request a matter to be included on the agenda of the General Meeting of Shareholders. Such requests, if sufficiently substantiated and received by the Company at least sixty days before the date of the meeting, can only be refused on the grounds of exceptional circumstances, to be checked against the principles of reasonableness and fairness.

All shareholders and other persons who, pursuant to Dutch law or the Articles, are entitled to attend and/or vote at a General Meeting of Shareholders are entitled to address the General Meeting of Shareholders. X5 uses the Bank of New York Mellon, the depositary for X5's GDR facility, to enable GDR holders to exercise their voting rights represented by the shares underlying the GDRs. As described in the "Terms and Conditions of the Global Depositary Receipts", holders of GDRs may instruct the Depositary with regard to the exercise of the voting rights connected to the shares underlying their GDRs. Alternatively, upon request of the holders of such depositary receipts, the Depositary will grant a proxy to such holders who wish to vote in person at a General Meeting of Shareholders. Persons who hold a written proxy may represent shareholders at a General Meeting of Shareholders. The written proxy must be duly executed and legalised in accordance with the applicable laws, and may be submitted electronically.

On 1 July 2010 a bill on shareholders' rights came into force in the Netherlands, implementing the European directive on the exercise of rights of shareholders in listed companies. Apart from certain rules reflected in this section, the new bill introduces amendments relating to publication and content of the notice for a shareholders' meeting, publication of voting results and further rules on circulation of information. At the 2011 Annual General Meeting of Shareholders, X5's shareholders will be requested to approve the amendment of the Company's Articles of Association in accordance with the new bill on shareholders' rights.

### **Voting Rights**

Each share confers the right to cast one vote at the General Meeting of Shareholders. There are no restrictions, either under Dutch law or in the Articles, on the right of non-residents of the Netherlands or foreign owners to hold or vote the shares, other than those also imposed on residents of the Netherlands. Resolutions of the General Meeting of Shareholders will be passed





by a simple majority of the votes cast in a meeting where more than 25% of the issued share capital is present or represented. If 25% or less of the issued share capital is present or represented, a second meeting should be convened and held no later than four weeks following the first meeting. At such second meeting, no quorum requirement will apply. However, the General Meeting of Shareholders can only resolve on a merger or demerger with a majority of at least two-thirds of the votes cast, if less than fifty percent of the issued capital is represented in that meeting.

**Dividend Rights**

Any distribution of profits to shareholders will be made after the adoption by the General Meeting of Shareholders of the annual accounts of the Company from which it appears that such distribution is permitted. The Company may only declare profit distributions insofar as its net assets exceed the sum of its issued share capital plus any legal reserves required to be maintained pursuant to Dutch law and the Articles. A loss may only be applied against such reserves to the extent permitted by Dutch law. On a proposal of the Supervisory Board, the General Meeting of Shareholders will determine which part of the profits will be added to the reserves and the allocation of the remaining profits.

On a proposal of the Supervisory Board, the General Meeting of Shareholders may resolve to pay an interim dividend insofar as X5's net assets exceed the sum of its issued share capital and

the reserves that are required to be maintained pursuant to Dutch law, as evidenced by an interim financial statement prepared and signed by all the members of the Management Board. In addition, on a proposal of the Supervisory Board, the General Meeting of Shareholders may resolve to make distributions to the shareholders out of any reserves that need not to be maintained pursuant to Dutch law.

Dividends and other distributions that have not been claimed within five years after the date on which they became due and payable revert to the Company.

**Significant Ownership of Voting Shares**

According to the Dutch Financial Markets Supervision Act (Wet op het financieel toezicht), any person or legal entity who, directly or indirectly, acquires or disposes of an interest in X5's capital and/or voting rights must immediately give written notice to the Netherlands Authority for the Financial Markets ('AFM'), if the acquisition or disposal causes the percentage of outstanding capital interest and/or voting rights held by that person or legal entity to reach, exceed or fall below any of the following thresholds: 5%, 10%, 15%, 20%, 25%, 30%, 40%, 50%, 60%, 75% and 95%.

The following table lists the shareholders on record on 10 March 2011 in the AFM's public register that hold an interest of 5% or more in the share capital of the Company:

Shareholder	Date of Disclosure	Capital Interest and Voting Rights <sup>(1)</sup>
CTF Holdings Ltd.	2 August 2007	47.86%
Axon Trust	22 December 2009	11.43%
The Baker Trust	11 December 2009	8.42%

<sup>(1)</sup> In accordance with the filing requirements the percentages shown include both direct and indirect capital interests and voting rights. Further details can be obtained at [www.afm.nl](http://www.afm.nl).





### Securities Owned by Board Members

The members of the Management Board and Supervisory Board and X5's other senior management are subject to the Company's Code of Conduct with regard to Insider Trading, which contains rules of conduct to prevent trading in X5's Global Depositary Receipts of shares or other financial instruments when holding inside information. The Code of Conduct with regard to Insider Trading can be viewed on the Company's website.

The Code of Conduct includes a specific section on obligations of members of the Management Board to report to the Compliance Officer in case of changes in their holding of securities in any Dutch listed company, not being X5 securities, in accordance with the Dutch Corporate Governance Code.

Furthermore, under the Dutch Financial Markets Supervision Act, members of the Management Board and Supervisory Board shall notify the AFM of X5 securities and voting rights at their disposal. These positions can be viewed on the AFM's public register.

In addition, under the Disclosure and Transparency Rules in the United Kingdom, X5 must notify a Regulatory Information Service (RIS) of the occurrence of all transactions in X5 conducted – on their own account – and notified by members of the Management Board and Supervisory Board.

### Repurchase by the Company of Its Own Shares

The Company may acquire fully paid shares, or depositary receipts thereof, in its capital for a consideration only following authorization of the General Meeting of Shareholders and subject to certain provisions of Dutch law and the Company's Articles of Association, if:

- › Shareholders' equity minus the purchase price is not less than the sum of X5's issued and fully paid-in capital plus any reserves

required to be maintained by Dutch law or X5's Articles of Association; and

- › X5 and its subsidiaries would not, as a result, hold shares or depositary receipts thereof with an aggregate nominal value exceeding half of the issued share capital.

The Management Board has been authorized to acquire up to 10% of the shares or depositary receipts thereof. This authorization is valid through 25 December 2011. In addition, the Supervisory Board has resolved that in case a purchase of shares or depositary receipts thereof by X5 would lead to X5 holding more than 5% of the shares or depositary receipts thereof, the Management Board requires the Supervisory Board's prior approval for such purchase.

Authorization by the General Meeting of Shareholders is not required if X5's own shares are acquired for the purpose of transferring those shares to X5 employees pursuant to any arrangements applicable to such employees.

Shares or depositary receipts thereof held by X5 or a subsidiary may not be voted on and are not taken into account for determining whether quorum requirements, if any, are satisfied.

### Issue of New Shares and Pre-Emptive Rights

Shares in X5 may be issued, and rights to subscribe for shares may be granted, pursuant to a resolution of the General Meeting of Shareholders or another corporate body of X5 to which the General Meeting of Shareholders has delegated such authority for a time not exceeding five years. The General Meeting of Shareholders approved a delegation of this authority to the Supervisory Board, relating to the issuance and/or granting of rights to acquire up to 16,226,820 shares (23.90% of the issued share capital) through 25 December 2011.



Upon the issue of new shares, holders of X5's shares have a pre-emptive right to subscribe for shares in proportion to the aggregate amount of their existing holdings of X5's shares. According to the Company's Articles of Association, this pre-emptive right does not apply to any issue of shares to employees of X5 or a group company. Pre-emptive rights may be restricted or excluded pursuant to a resolution of the General Meeting of Shareholders or another corporate body of X5 to which the General Meeting of Shareholders has delegated such authority for a time not exceeding five years. The General Meeting of Shareholders has delegated the authority to restrict or exclude the pre-emptive rights of shareholders upon the issue of shares and/or the granting of rights to subscribe for shares to the Supervisory Board through 25 December 2011.

#### **Articles of Association**

X5's Articles of Association contain rules on organization and corporate governance of the Company. The current text of the Articles of Association is available at the Trade Register of the Chamber of Commerce and Industry for Amsterdam and on X5's website.

The amendment of the Articles of Association of the Company requires a resolution of the General Meeting of Shareholders. The proposal to amend the Articles including the text of the proposed amendment must be made available to holders of shares and GDR holders for inspection at the offices of X5 as of the date of the notice convening the meeting of the General Meeting of Shareholders until the end of the meeting of the General Meeting of Shareholders at which the proposed amendment is voted on.

At the 2011 Annual General Meeting of Shareholders, X5's shareholders will be requested to approve the amendment of the Company's Articles of Association in accordance with the new

Dutch bill on shareholders' rights which came into force on 1 July 2010, implementing the European directive on the exercise of rights of shareholders in listed companies.

#### **Auditor**

The General Meeting of Shareholders appoints the external auditor upon nomination of the Supervisory Board. Both the Audit Committee and the Management Board make a recommendation to the Supervisory Board with respect to the external auditor to be proposed for (re)appointment by the General Meeting of Shareholders. In addition, the Audit Committee evaluates and, where appropriate, recommends the replacement of the external auditor. The Audit Committee also pre-approves the fees for audit and permitted non-audit services to be performed by the external auditor as negotiated by the Management Board. The Audit Committee shall not approve the engagement of the external auditor to render non-audit services prohibited by applicable laws and regulations or that would compromise their independence.

At least every four years, the Management Board shall together with the Audit Committee thoroughly assess the functioning of the external auditor in the various entities and capacities in which the external auditor operates. The main conclusions of the assessment shall be notified to the General Meeting of Shareholders for the purpose of considering the nomination for the appointment of external auditor of the Company.

#### **Corporate Governance Code**

X5 is subject to the Dutch Corporate Governance Code (the "Code"), which came into effect on 1 January 2004. On 10 December 2008 the Dutch Corporate Governance Code Monitoring Committee (the "Committee") presented an amended Code, which became effective on 1 January 2009. The full text of the amended Code can be viewed on X5's website.



Some of the Code's best practice provisions have been incorporated into Dutch law, including the obligation for a listed company to state each year in its annual report how it applied the recommendations of the Code in the past financial year and to explain carefully, where applicable, why a provision was not applied in circumstances where the listed company departed from the recommendations of the Code.

X5's corporate governance policy with respect to the implementation of the Code was last discussed with its shareholders at the 2010 Annual General Meeting of Shareholders. Since then, there were no substantial changes in the corporate governance structure of the Company. X5 generally adheres to the Code, as amended, but does not comply with the following recommendations:

#### **II.2.4: Grant of Options to Members of the Management Board**

Pursuant to the Code, if a company grants options to members of its management board, such grant should be subject to certain performance criteria and the options should not be exercisable within three years following the date of grant.

On 15 June 2007, the General Meeting of Shareholders approved the Company's Employee Stock Option Plan (the "ESOP"), under which options are granted to employees in four tranches over a period of three years with varying vesting periods. The vesting requirement of the programme is the continued employment of participants. The final tranche of options under the ESOP vested on 19 May 2010.

While the ESOP is considered a long-term compensation for its participants, and the grant of options was linked to pre-determined, measurable performance based targets, X5 acknowledges that in terms of vesting period the ESOP

deviates from the Code. However, since X5's operational activities are mainly based in the Russian Federation and the Ukraine, and the grant of unconditional options with a shorter than three year vesting period was customary in these markets at the time the ESOP was designed (2007), it was important for X5 to deviate on this point from the Code in order to attract and reward the best professionals in these markets.

The Company's next generation long-term incentive plan launched in 2010 (the "Restricted Stock Unit Plan", see Remuneration Report on page 75) provides for vesting and lock-in periods in line with the Code's best practices.

#### **II.3.4, III.6.3 and III.6.4: Disclosure of Transactions with Related Parties in the Annual Report**

In accordance with the Code, transactions with members of the Management Board, Supervisory Board, or persons holding at least 10% of shares or depository receipts thereof in which there are significant conflicting interests will be published in X5's Annual Report. However, in deviation from the Code, a detailed statement of the relevant conflict of interest is not published if (i) this conflicts with the law, (ii) the confidential, share-price sensitive or competition-sensitive nature of the transaction prevents publication and/or (iii) the information is so competition-sensitive that the publication could damage X5's competitive position.

#### **III.2.1: Independence of Members of the Supervisory Board**

Pursuant to the Code, all, but one, of the members of the Supervisory Board must be independent.

Three out of seven members of the Supervisory Board have a substantial shareholder interest in X5, or are related to companies that are owned or controlled by companies that



ultimately hold 10% or more of the shares or GDRs in X5. These members of the Supervisory Board are, therefore, not considered to be independent within the meaning of the Code. Mr. Hervé Defforey, Mr. Alexander Tynkovan, Mr. Stephan DuCharme and Mr. Christian Couvreur are independent within the meaning of the Code.

X5 believes that the non-independent members of the Supervisory Board have an in-depth knowledge of the geographic market, of business in general and of retail specifically in the markets in which X5 operates, which is of particular advantage to X5 and its stakeholders.

### **III.5: Committees of the Supervisory Board and Deviation from the Maximum of One Non-Independent Member of the Audit Committee**

In 2009, the Supervisory Board resolved to merge the Supervisory Board's Remuneration Committee and Selection and Appointment Committee to one 'Nomination and Remuneration Committee.' X5 currently deviates from the Code, which requires these two committees to be separate committees. However, in light of the respective duties, responsibilities and composition of each of the Remuneration Committee and the Selection and Appointment Committee, and for reasons of practicality, X5 believes that it was in X5's best interest to merge these Committees.

In addition, X5 acknowledges that Mr. David Gould and Mr. Vladimir Ashurkov are non-independent members of the Audit Committee within the meaning of the Code whereas,

pursuant to the Code, the terms of reference of each committee of the Supervisory Board may provide that a maximum of one member of each committee may not be independent. Considering Mr. David Gould's and Mr. Vladimir Ashurkov's financial expertise, and for reasons of continuity, X5 believes that it is in X5's best interest that Mr. David Gould's and Mr. Vladimir Ashurkov's membership of the Audit Committee be continued.

### **III.7.1: No Grant of Shares and Options to Members of the Supervisory Board**

Pursuant to the Code, members of the Supervisory Board shall not be granted any shares and/or rights to subscribe for shares as remuneration for their membership of the Supervisory Board.

On 15 June and 5 November 2007, 16 June 2008 and 15 January 2010 the General Meeting of Shareholders approved the granting of options to Mr. Hervé Defforey and Mr. Stephan DuCharme, both members of the Supervisory Board. Furthermore, on 25 June 2010, the General Meeting of Shareholders approved the conditional grant of Restricted Stock Units to the Supervisory Board members Mr. Hervé Defforey, Mr. David Gould, Mr. Alexander Tynkovan, Mr. Stephan DuCharme and Mr. Christian Couvreur. X5 acknowledges that such grants deviate from the Code. However, in order to attract and reward experienced individuals with a track record that is of specific relevance to the Company, X5 believes it is necessary to allow members of the Supervisory Board to participate in the Company's long-term incentive plans.