Committee will contribute to the achievement of MSV and a compensation plan that truly contributes to the establishment of an executive philosophy.

Nakamura

Takashi Tsutsui was elected Independent Director of NPHD in March 2018, serving as the Compensation Committee Chairperson. Thanks to his many years of experience in executive career design, he played an important role in formulating Compensation Philosophy and in a reform of the executive compensation plan that aims to achieve MSV. Mr. Tsutsui has ample experience in global business operations for around 30 years at listed companies including Nomura Securities Co., Ltd. and has a keen insight into corporate governance.

We believe that our executive compensation plan is also undergoing a major transformation. The Compensation Committee members have been and will continue to adhere to “what compensation plan will contribute to MSV.” As we drive this transformation, Mr. Tsutsui, the Compensation Committee Chairperson, and I will look back on why we considered the executive compensation plan developed by the Compensation Committee will contribute to the achievement of MSV and what were the discussions we held towards creating such a plan.

Tsutsui • Well, compensation design needs to maintain some degree of continuity. It is not necessarily a good idea to suddenly switch our compensation plan to an ideal one. Naturally, we need to develop a compensation plan that is fair and rational and can fulfill accountability requirements by taking into account objective information and specialized advice by making use of the help of external advisors and other parties. Also, an ideal compensation plan should be able to adapt to the company’s growth stage and the social circumstances in which it operates. I don’t think there is any single perfect goal that always applies.

It may be a roundabout way of explaining our conclusion “what compensation plan will contribute to MSV” but let us begin by retracing our footsteps.

Nakamura • Mr. Tsutsui and I were elected as Directors of NPHD at the General Meeting of Shareholders in March 2018. NPHD, then was a “Company with a Nominating Committee, etc.” structure in March 2020. As you know, in August 2020, we decided to fully include the Asian JV’s, which had grown to account for roughly 50% of the consolidated revenue and over 60% of the consolidated operating profit, into the consolidation by acquiring their remaining 49% equity stakes.

Decision to acquire the Indonesia business was also taken at the same time. Those events required a major transformation of management teams and their compensation to take the Group to the next growth stage. It was also in 2019 that the Compensation Philosophy was established.

Now, let us look back at NPHD’s initiatives for business expansion and changes in the structure of our compensation design for the President in terms of timelines. First, the period “Up until the full integration of the Asian JVs (2018-2020)” and second, the period “From the full integration of the Asian JV’s to the adoption of the Co-President structure (2021-2022)” Then we will turn our thoughts to “our vision for the future.”

Tsutsui • It may be misleading, but my first impression was that NPHD’s executive compensation plan was an ordinary

Toward the establishment of an executive compensation plan that truly contributes to Maximization of Shareholder Value (MSV)

Why we considered the executive compensation plan compensation system developed by the Compensation Committee will contribute to the achievement of MSV and what were the discussions we held toward creating such a plan? — On this page, Independent Directors, Masayoshi Nakamura (Board Chair) and Takashi Tsutsui (The Compensation Committee Chairperson), look back at previous discussions held at the Compensation Committee and explain how the optimal executive compensation plan is contributing to MSV, the role of the Compensation Committee, and their thoughts about the design of the compensation plan for the future.

Retracing the footsteps of the Compensation Committee

Nakamura • It has now been over a year since we adopted the Co-President structure on April 28, 2021. Mr. Wae-Suw Kim, one of the Co- Presidents, is a Singaporean residing in Singapore, and he became the first non-Japanese president of the company under the current Co-President structure. In early 2022, we announced the adoption of Asset Assembler model for pursuing MSV. By those actions, we have taken the group management to the next stage.

Tsutsui • Well, compensation design needs to maintain some degree of continuity. It is not necessarily a good idea to suddenly switch our compensation plan to an ideal one. Naturally, we need to develop a compensation plan that is fair and rational and can fulfill accountability requirements by taking into account objective information and specialized advice by making use of the help of external advisors and other parties. Also, an ideal compensation plan should be able to adapt to the company’s growth stage and the social circumstances in which it operates. I don’t think there is any single perfect goal that always applies.

It may be a roundabout way of explaining our conclusion “what compensation plan will contribute to MSV” but let us begin by retracing our footsteps.

Nakamura • Mr. Tsutsui and I were elected as Directors of NPHD at the General Meeting of Shareholders in March 2018. NPHD transitioned to “a Company with a Nominating Committee, etc.” structure in March 2020. As you know, in August 2020, we decided to fully include the Asian JV’s, which had grown to account for roughly 50% of the consolidated revenue and over 60% of the consolidated operating profit, into the consolidation by acquiring their remaining 49% equity stakes.

Decision to acquire the Indonesia business was also taken at the same time. Those events required a major transformation of management teams and their compensation to take the Group to the next growth stage. It was also in 2019 that the Compensation Philosophy was established.

Now, let us look back at NPHD’s initiatives for business expansion and changes in the structure of our compensation design for the President in terms of timelines. First, the period “Up until the full integration of the Asian JVs (2018-2020)” and second, the period “From the full integration of the Asian JVs to the adoption of the Co-President structure (2021-2022)” Then we will turn our thoughts to “our vision for the future.”

Tsutsui • It may be misleading, but my first impression was that NPHD’s executive compensation plan was an ordinary

Compensation Philosophy

Overarching Principle

• In order to implement MSV, to build a compensation plan that is transparent and satisfactory and to continue to provide appropriate motivation and incentives to key executives by implementing individual treatment based on the plan.

Guiding Principles

• To be able to attract and keep management talent that excels at practicing MSV.

• To be able to continuously provide motivation so that maximum potential can be encouraged even under changing environments.

• To function effectively and in harmony with the current state of business development, level of maturity of organizational systems, organizational values, and the community.

Design Policies for the Compensation of the Representative Executive Officer and Co-Presidents

• Compensation that contributes to MSV

• Total compensation is commensurate with the performance of the Representative Executive Officers & Co-Presidents

• A compensation structure that promotes appropriate and decisive risk-taking

“Up until the full integration of the Asian JVs” (2018-2020)

What kind of executive compensation plan was necessary to prepare for the full integration of the Asian JVs?

Nakamura • At the time we were elected as Directors, our committee was the Compensation Advisory Committee based on the corporate governance structure of “a Company with a Board of Company Auditors.” What was your first impression of the executive compensation plan and the issues if faced when you were initially briefed? Tsutsui • It may be misleading, but my first impression was that NPHD’s executive compensation plan was an ordinary
executive compensation plan of Japanese companies without any special features. We both already had a clear vision when we became the Directors that it would be an inevitable decision for NPHD to fully integrate the Asian JVs in the near future to achieve MSV and we had to prepare for this and, at the same time, guide the executives to make that decision.

Based on the executive compensation plan back then, the President’s total compensation exceeded 100 million yen and the plan included short-term incentives (STI) in the form of performance-linked compensation and long-term incentives (LTI) through stock options. However, based on what we had in our mind as an ideal executive compensation plan, we thought something was missing—it needed a new approach, and one that was not limited by conventional arrangements in order to boost the motivation and incentives of the President and other senior managers to achieve MSV.

Nakamura* had the same view. He visualized a President who would make the decision on the full integration of the Asian JVs or a President who would drive the globalized Nippon Paint Group to the next growth stage following the full integration of the Asian JVs. Then, thinking what kind of compensation plan would be appropriate for this person, I felt that NPHD would not be able to attract the person it required under the existing compensation plan.

Tsutsui: That’s right. What we needed was an executive compensation plan that met the needs of all the management teams, from the President and other executives to bring out their maximum potential. If the right candidate is outside the Group, it should be able to attract and retain that person. Accordingly, we proceeded to reform it, focusing on “working out a satisfactory total amount of compensation, raising our compensation to a competitive level,” and “designing a compensation structure that requires a clear commitment by the President to achieving MSV.” That said, if we were to determine compensation as the occasion demanded, we would be naturally required to determine compensation that is commensurate with the performance of the President in office at that time. While applying a strict performance assessment for the President, we proactively adopted a new approach to the compensation of the President’s compensation, by means such as increasing the proportion of stock-based compensation. In this manner, we enhanced our compensation plan in terms both of the total amount and of the composition of the compensation.

Nakamura: As a result of those compensation reforms, we increased the compensation for the President in FY2020, when NPHD shifted to “a Company with a Nominating Committee, etc.” structure by around three times. The Compensation Committee members are Co-Presidents, who are responsible for evaluating the President and other executives to bring to the group management as an understanding by the Compensation Committee that suits each region and business based on standardized compensation structure. Rather, it is important to comprehensively evaluate the performance and contributions at that point, even if the Co-Presidents make a report to the Compensation Committee meetings. These discussions culminated in our Compensation Philosophy.

Our next move to create compensation plans with agility and a sense of vigilance. We achieved MSV at a time when the Group is facing significant challenges, and we believe that the leadership of the President and other executives to bring to the group management as an understanding by the Compensation Committee that suits each region and business based on standardized compensation structure.

The Compensation Philosophy

Tsutsui: During this time, we certainly increased the compensation for the President. This reflects an appropriate evaluation and recognition of the President’s job responsibility and performance, while the same time incorporating the tough requirements that are expected in return. I can proudly say that our stance is reflected in our Compensation Philosophy (See page 113). What I would like to emphasize, especially regarding the compensation design that we laboriously developed, is the following: The compensation for the President in FY2020 was comprised of job-based compensation as a fixed compensation accounting for around 40% of the total compensation.
Nakamura • So far, we have been looking back at our thoughts about the compensation for the President. What is required of Independent Directors is the same; in that our performance is always subject to shareholders’ scrutiny.

Tsutsui • Indeed. Although business execution is not a part of our role, we not only supervise the group management as an Asset Assembler but also assume the role and risk involved in making important decisions regarding the allocation of management resources entrusted to us by our shareholders. We believe that it is important to further enhance value sharing with shareholders, in other words, incentives for achieving MSV. That’s why we have introduced stock-based compensation plans such as fixed compensation for the Directors who do not serve concurrently as Executive Officers. This is restricted stock compensation that cannot be sold during the term of office. Also, Maia and扫黑 clauses are in place, enabling the Independent Directors to properly share values with our shareholders, especially minority shareholders.

Nakamura • I believe that our compensation plan for Independent Directors is appropriate for a company that sees MSV as its sole mission. Specifically, the current compensation for Independent Directors is equally divided between cash and restricted stock. In principle, when the restriction is lifted after Independent Directors retire from their office, they have almost nothing left, except NPISH’s stock, net of tax. In other words, the only incentive the Independent Directors receiving the restricted stock have is to boost NPISH’s stock price continuously, both during their terms of office and after their retirement. The difference before our election and after our retirement as NPISH’s Independent Directors is an important indicator that we will have truly become minority shareholders of NPISH.

Tsutsui • That is how we have designed the compensation for Independent Directors. In order for the Group to expand operations globally through M&A based on Asset Assembler model and to build a really sustainable management base to achieve MSV, with all possible concerns for the Group eliminated, Independent Directors must not only supervise the Group’s management from both ‘independent and outside’ perspectives, but also be committed to devoting a considerable amount of their time and maintaining close and excellent discussions on individual agenda items requiring management decision-making. Considering these points, I believe that it is an appropriate compensation composition for NPISH’s Independent Directors to include stock-based compensation.

“From the full integration of the Asian JVs to the adoption of the Co-President structure” (2021-2022)

Nakamura • We were able to reflect on the discussions and issues surrounding our executive compensation plan that culminated in our Compensation Philosophy. I would now like to take a fresh look at the new reform initiatives of the Compensation Committee to prepare for transition to the current Co-President structure.

Discussions centered on evaluating and determining compensation for the President

Nakamura • I believe that the Compensation Committee worked from the premise that we should focus on the evaluation and determination of the compensation for the President, who is the head of the Company. Therefore, we have separately established the “Design Policies for the Compensation of the Representative Executive Officers and Co-President Compensation” (see page 121) in compliance with the Compensation Philosophy. First, let us outline the background of this concept.

Tsutsui • Since our election as Directors, we have envisioned a business model for Nippon Paint Group of expanding its operations for even further growth globally, considering the characteristics of its business areas centered on paint and coatings. What we had in mind specifically was a business model in which NPISH will attract partner companies around the globe and drive growth at each partner company by essentially entrusting these companies with autonomous management based on trust.

The key to the success of this growth model is unquestionably, the Co-Presidents of NPISH, which is a pure holding company. Therefore, the Compensation Committee determined that the evaluation and determination of compensation for the Co-Presidents be our most important role. We needed to establish a compensation plan that would strongly support the group management led by the Co-Presidents. In the meantime, we decided to delegate to the Co-Presidents the responsibility for evaluating and determining the compensation for the management teams of partner companies.

Nakamura • These discussions led to the development of the current Asset Assembler model. We thought the key parameters for properly evaluating the performance of the Co-Presidents would be: “how well the Co-Presidents lead other Executive Officers, and Global Key Persons (GKPs), who are the key management teams of partner companies,” and “how well they determine compensation for GKPs.”

Tsutsui • I believe that is at the core of our approach to the evaluations we will perform.

The Compensation Committee is responsible for evaluating the performance and determining the compensation of the Executive Officers, including the Co-Presidents. The prerequisite for our evaluation of the Co-Presidents is an understanding by the Compensation Committee members of the personalities and performance of the Co-Presidents, as well as GKPs, including the Executive Officers.

Therefore, we have established a procedure by which the Co-Presidents report to the Compensation Committee on how they manage and evaluate other Executive Officers and GKPs, while the Compensation Committee evaluates and determines the compensation for the Co-Presidents and other Executive Officers after carefully considering the content of reports from the Co-Presidents.

Every partner company has its own business practices of each region. Based on Asset Assembler model, we do not impose a standardized compensation structure. Rather, we are required to work with the Co-Presidents to explore a better direction that suits each region and business based on a deep understanding of the uniqueness of each partner company. We believe the Co-Presidents need to think about whether the best approach to evaluation and compensation decisions using a formula that can quickly reflect the current business environment and other situations. Even if the performance and contributions at that point, it is not right to make decisions based solely on the degree of achievement of numerical targets, nor is it right to do so by taking the reports from the Co-Presidents at face value. The important thing is to evaluate a person’s value as a manager from multi-faceted perspectives and so to understand the merit of each person.

Nakamura • Adequate communication is essential for this purpose, and both the Nominating Committee and the Audit Committee have been working on expanding communication with GKPs.

The Audit Committee follows an “Audit on Audit” system, in which our partner companies are grouped by business region and NPISH audits the status of auditing within each group. The Audit Committee also interviews each GKP on a regular basis. The meetings of Independent Directors, where I serve as the Chairperson, have also spent time to increase communication with GKPs through meetings over lunch and on other occasions.

The qualitative information and relationship building that these opportunities provide is invaluable for the Board of Directors in understanding the Group’s human capital at the senior management level that goes beyond the scope of the Committees.
Going beyond formula-based compensation decisions

Nakamura • Through these communications, we have made an effort to assess the merits of the Co-Presidents and other Executive Officers. We have also had many discussions on whether we should reflect the results of evaluations based on this assessment for making compensation decisions.

Tsutsui • Under the executive compensation plan that was in place prior to our election as Directors, the amount of performance-linked compensation for the President was automatically calculated by using a formula that used consolidated net sales and profit before tax as indicators.

This compensation is linked directly to Nippon Paint Group’s performance and had the advantage of being fair and transparent to some degree. However, we didn’t think that it was really the best way to evaluate the performance of executives, nor did we think that each member of the management team would be convinced that their performance had been properly evaluated and recognized. We thought that calculating and determining the compensation based on formulas have limitations because Nippon Paint Group must respond with agility to the rapid changes in business environment, which have been exacerbated by the pandemic. Therefore, we continued to explore an optimal evaluation and compensation determination method that can quickly reflect the current business climate.

Nakamura • I believe this is the core of the transformation, led by the Compensation Committee, from the conventional “evaluation and compensation decisions using a position-based fixed compensation table” to “compensation decisions based on comprehensive evaluations.”

Based on our activities to enhance the compensation for the President in terms of both the total amount and composition, we decided to comprehensively evaluate the performance of the Co-Presidents through dialogues with them and close communications with GKPs for determining their compensation in FY2021. We also decided that total compensation, starting in FY2022, will be determined every year from the ground up and the percentages of cash and stock-based compensation will be reviewed every year.

Tsutsui • We often hear people say that compensation based on a clearly defined formula makes it more transparent as performance-linked compensation. However, Nippon Paint Group is undergoing drastic transformations. Group companies establish initial plans and budgets as well as KPIs from both financial and non-financial perspectives. We have held many discussions on whether compensation decisions using a formula based on company business plans would really work as an appropriate incentive to achieve MSV at a time when the Group is undergoing growth amid drastic changes in the business environment.

It is our responsibility to strongly support the Co-Presidents as they review business plans with agility and a sense of vigilance. We must also support their relentless pursuit of major goals and by extension growth to achieve MSV. We intend to work with the Co-Presidents to determine actions that are needed to keep changing based on the concept of MSV.

Nakamura • This may not be a good analogy, but members of the Compensation Committee were thinking about the fact that “An officer going to the war is not asked to only follow predetermined KPIs or review KPIs every time.” Willis Towers Watson, which is our external compensation advisor, commented that we are oriented toward the ODCA (Oriente, Orient, Decade, Act) model, which is more flexible and responsive to different situations, rather than the PDCF (Plan, Do, Check, Act) model, which requires careful planning.

Tsutsui • We constantly discuss group activities more often at the Board of Directors meetings than at the Compensation Committee meetings. These discussions involve both financial indicators and non-financial indicators, such as ESG and sustainability performance.

However, we do not believe that we can arrive at the compensation plan we seek to achieve by simply calculating compensation by doing additions and subtractions based on the degree of attainment of KPI targets. For example, we could add 5 points because performance exceeded the initial target by 5% for a particular KPI involving ESG.

Rather, it is important to comprehensively evaluate each individual’s actions, performance and contributions at that point, taking into consideration the changing environment and other situations. Even if revenue and profits decline, for instance, we may give someone a positive evaluation if the decrease was caused by external factors and the market share increased despite the decline. On the contrary, we may give someone a negative evaluation even when revenue and profit increase if the benefits of price increases to reflect higher expenses did not emerge in a timely manner.

We believe that a comprehensive evaluation that carefully examines performance will serve as a proper incentive for executives to maximize their performance, as well as lead to the retention of these people.

Nakamura • The compensation for the Co-President is based solely on a comprehensive evaluation by the Compensation Committee, and total compensation for the following year will be reviewed from the ground up. Therefore, the Co-Presidents’ compensation consists entirely of variable compensation. From the standpoint of people being evaluated, this may be a very demanding compensation plan.

For this compensation system to really function properly, the prerequisite is that we win the trust of the Co-Presidents that our judgments will definitely lead to MSV. I am convinced that the relationship we have developed with them through communications and the mutual trust backed by our track record will be the driving force behind our compensation plan.

Our vision for the future

Nakamura • We have covered the main topics that we considered and discussed leading up to the current Co-President structure. From here on, I would like to summarize our thoughts looking to the future.

What kind of compensation is conducive to sharing value with our shareholders?

Tsutsui • When considering our future compensation design, I believe we should place even more emphasis on determining what kind of compensation is truly conducive to raising incentives for achieving MSV and furthering value sharing with shareholders.

Nakamura • From that perspective, there is also the question of who should share value with shareholders in the first place. We also need to think about whether the best approach is holding stock, receiving stock as compensation, having compensation linked to the stock price, and so on.

Tsutsui • Directors are directly elected by shareholders. Therefore, it is obvious that we need to share value especially with minority shareholders. From a global perspective, there are many examples of companies that establish shareholders’ guidelines for their presidents. Simply put, the Co-Presidents are subject to these guidelines. It is natural to believe that the shortest path to value sharing with shareholders is for the Co-Presidents to hold a significant number of shares of NPHD stock.

In this regard, we should either establish a policy that allows the Co-Presidents to purchase this stock or design our stock-based compensation in a suitable manner. But in reality, it’s not that simple.

Even if the Co-Presidents intend to purchase NPHD stock, they will definitely be exposed to material facts constantly as they become party to transactions. As a result, they are subject to these guidelines. It is natural to believe that the shortest path to value sharing with shareholders is for the Co-Presidents to hold a significant number of shares of NPHD stock.

In this regard, we should either establish a policy that allows the Co-Presidents to purchase this stock or design our stock-based compensation in a suitable manner. But in reality, it’s not that simple.

Even if the Co-Presidents intend to purchase NPHD stock, they will definitely be exposed to material facts constantly as they become party to transactions. As a result, they are subject to these guidelines. It is natural to believe that the shortest path to value sharing with shareholders is for the Co-Presidents to hold a significant number of shares of NPHD stock.

In this regard, we should either establish a policy that allows the Co-Presidents to purchase this stock or design our stock-based compensation in a suitable manner. But in reality, it’s not that simple.

Even if the Co-Presidents intend to purchase NPHD stock, they will definitely be exposed to material facts constantly as they become party to transactions. As a result, they are subject to these guidelines. It is natural to believe that the shortest path to value sharing with shareholders is for the Co-Presidents to hold a significant number of shares of NPHD stock.

In this regard, we should either establish a policy that allows the Co-Presidents to purchase this stock or design our stock-based compensation in a suitable manner. But in reality, it’s not that simple.

Even if the Co-Presidents intend to purchase NPHD stock, they will definitely be exposed to material facts constantly as they become party to transactions. As a result, they are subject to these guidelines. It is natural to believe that the shortest path to value sharing with shareholders is for the Co-Presidents to hold a significant number of shares of NPHD stock.

In this regard, we should either establish a policy that allows the Co-Presidents to purchase this stock or design our stock-based compensation in a suitable manner. But in reality, it’s not that simple.