

ARAG HOLDING SE

# 2016 Annual Report

CONSOLIDATED FINANCIAL STATEMENTS



Dive into life.

## The ARAG Group at a Glance

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Premium income/sales revenue:

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€ **1.78** billion

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↗ 2015: €1.72 billion

Combined ratio:

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**91.5** %

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↘ 2015: 92.3 %

Underwriting result for own account:

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€ **66.7** million

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↗ 2015: €66.1 million

Consolidated equity:

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€ **462** million

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↗ 2015: €426 million

Profit from ordinary activities:

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€ **87.0** million

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↗ 2015: €66.7 million

Consolidated net income:

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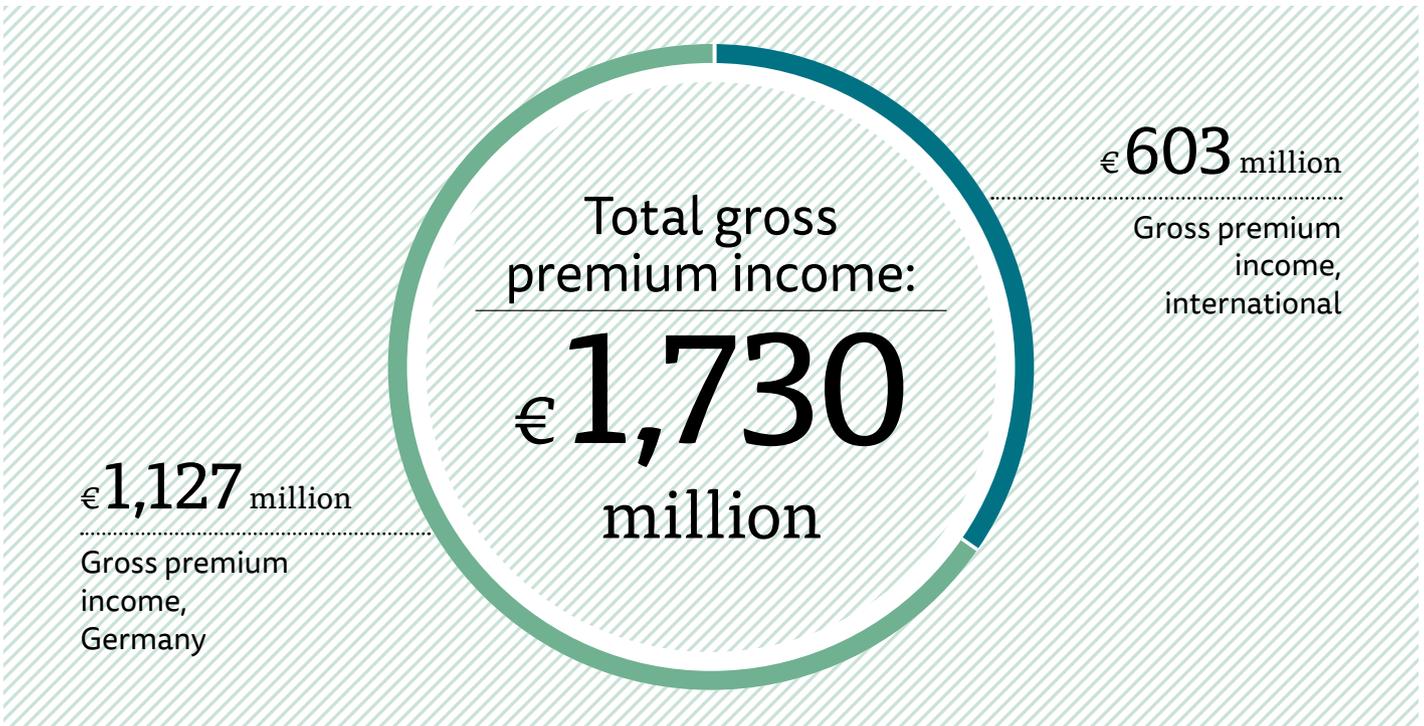
€ **43.1** million

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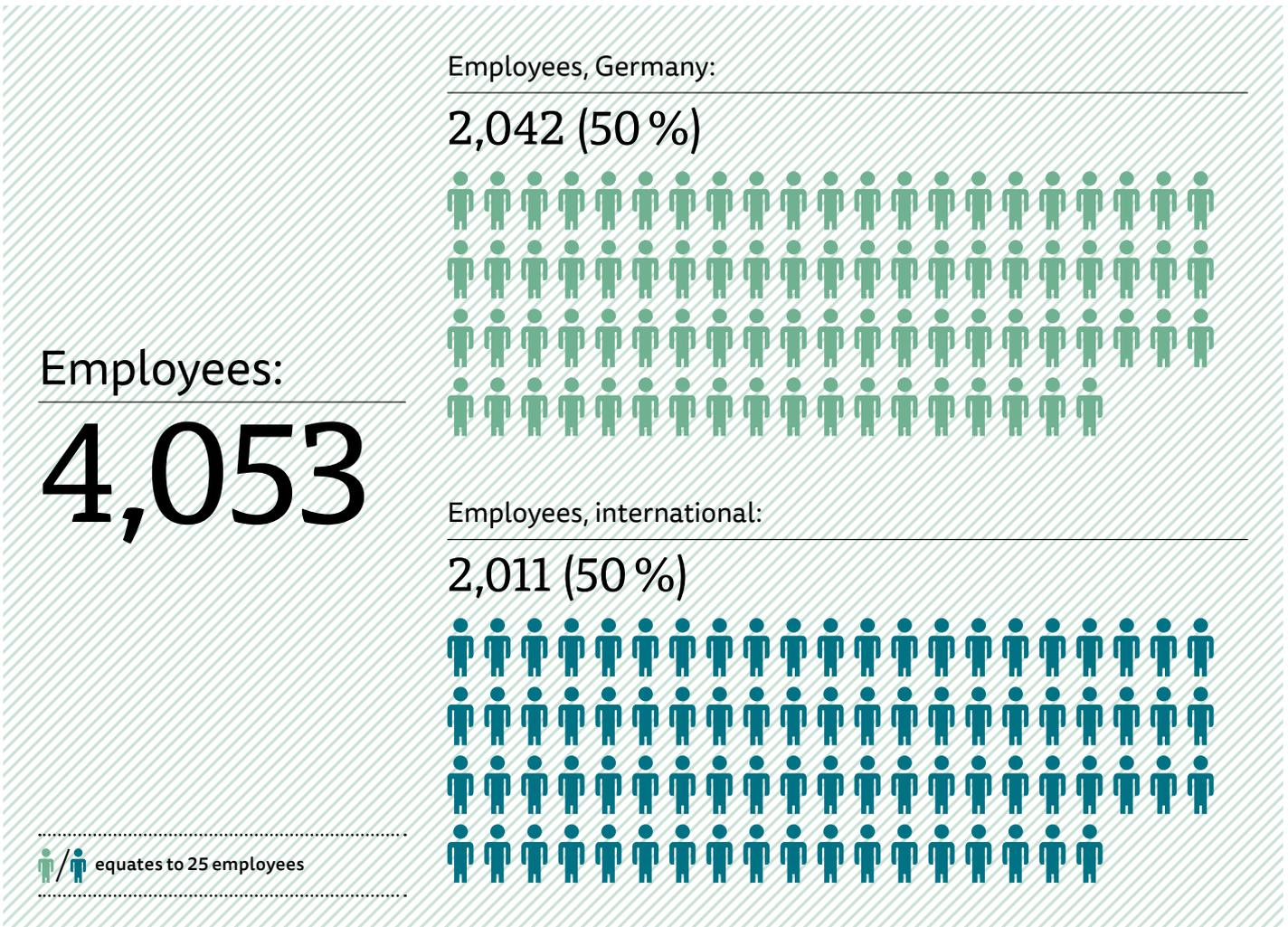
↗ 2015: €29.2 million

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Gross premium income broken down by domestic and international business



Number of employees and breakdown



## Insurance segments in the ARAG Group and their parent operating companies

### Legal insurance ARAG SE

€ 893 million\*

↗ 2015:

€ 842 million\*

Personal legal insurance and legal insurance for motorists, employment, homeowners and tenants, businesses, trades, self-employed professionals, and associations

### Casualty and property insurance ARAG Allgemeine Versicherungs-AG

€ 266 million\*

↗ 2015:

€ 247 million\*

Liability insurance, home contents insurance, accident insurance, accident disability insurance, Top Special Service Package, building insurance, business insurance, sports insurance

### Health insurance ARAG Krankenversicherungs-AG

€ 357 million\*

↗ 2015:

€ 347 million\*

Private full-coverage health insurance, supplementary health insurance, long-term nursing care insurance, supplementary nursing care insurance, corporate health insurance, foreign travel health insurance

### Life insurance ARAG Lebensversicherungs-AG

€ 214 million\*

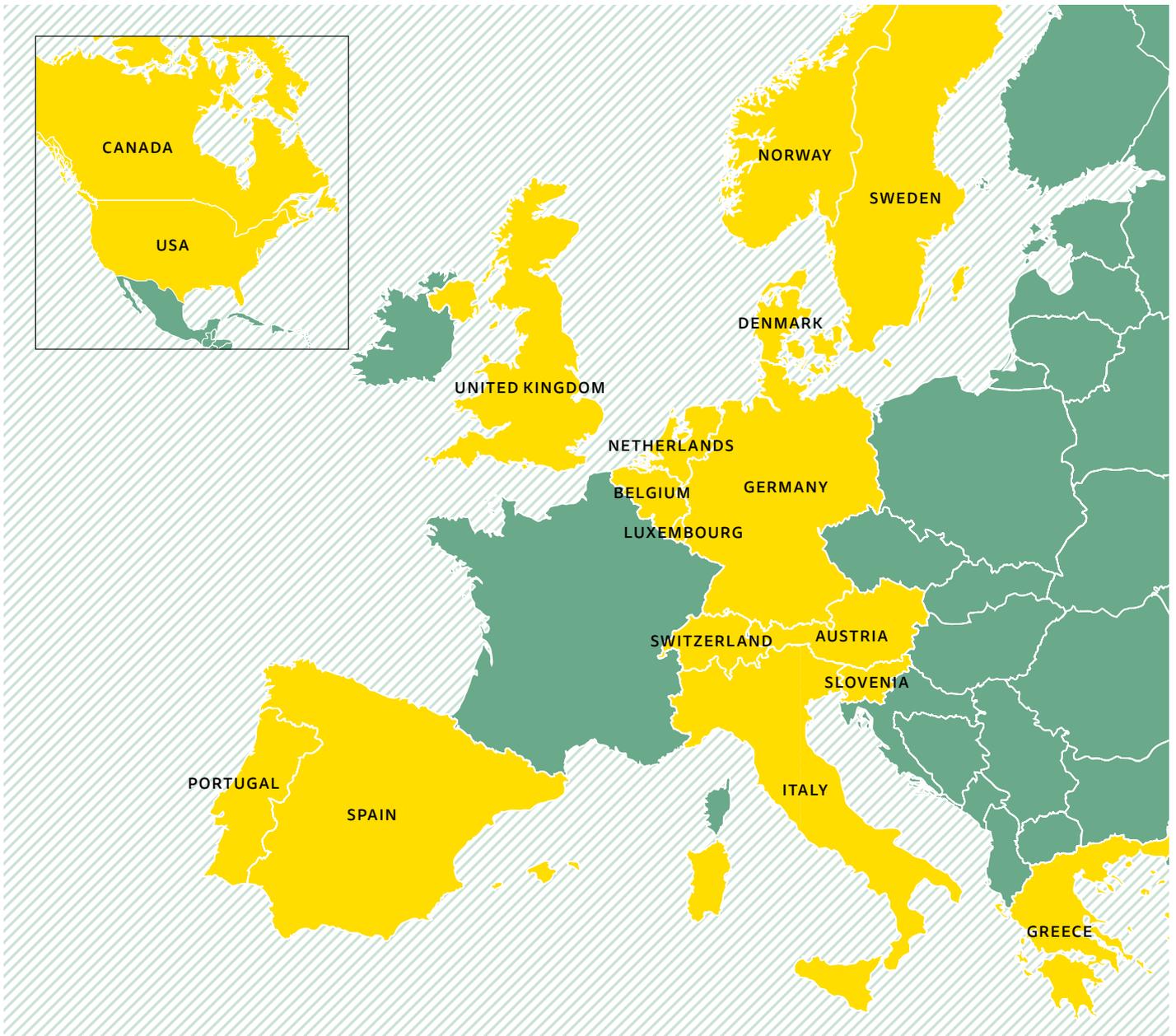
↘ 2015:

€ 220 million\*

Mutual-fund-linked pension insurance, private pension insurance (incl. Riester/Rürup plans), endowment life insurance, term life insurance, disability insurance, supplementary survivors' insurance and supplementary accidental death insurance, company pension plans

\* Gross premium income

## Countries in which the ARAG Group operates



## Accolades received by the ARAG Group (selection)

The 2015 ARAG Group annual report emerged as a **Bronze Winner Worldwide** in a competition run by the **League of American Communications Professionals (LACP)**. In the **Plus X Award** for innovation, ARAG premium legal insurance won the **Most Innovative Brand Award** in the insurance category. A **Golden Bull** (third place) from German financial publisher Finanzen was awarded to the ARAG Sofort legal insurance product for

motorists in the **insurance innovation of the year** category. In a study of the **best private health insurance providers of 2016** conducted by DFSI, a German financial services institute, ARAG health insurance came **third**. The Company was again voted by brokers as the most popular supplementary health insurance provider, taking **first place** in the **AssCompact Trends** awards for the **37th quarter in**

**succession**. Outside Germany, Spanish broker organization **ADECOSE** again designated ARAG Spain as **most popular legal insurer** and **most popular travel assistance company**. In the ranking of Spanish insurers' websites published regularly by **Innovación Aseguradora**, ARAG Spain's website occupied **second place** at the start of 2017. In the **third Italy Protection Awards**, ARAG Italy was chosen as **best insurer and reinsurer**

for legal insurance. The **MF Innovazione Award 2016** saw the ARAG Multioption product take **third place** in the multirisk category. ARAG plc in the UK was again crowned **Managing General Agents Team of the Year** and **Legal Expenses Team of the Year** in the **Underwriting Service Awards 2016**. In 2016, ARAG Netherlands received the **Keurmerk Klantgericht Verzekeren (KKV)** customer quality seal

of approval, which is awarded by the Dutch financial supervisor (Stv). **Benchmark-Portal** classified ARAG North America's customer center as one of its **top 100 call centers** for the sixth year in a row. Austrian financial magazine **Der Börsianer** voted ARAG Austria among the three **best specialist insurers in Austria**. In the **Assekuranz Award Austria**, ARAG Austria's private legal insurance was also rated **'very good'**.

# The ARAG Group

Asset and investment management

ARAG Holding SE

Operating Group Holding Company

ARAG SE

and legal insurance

Central Group Functions

Group Development, Business Organization

Group Sales

Products and Innovation

Group Finance

Group IT and Operations

Group Risk Management / Controlling

Operating insurance companies

ARAG Allgemeine Versicherungs-AG

(Casualty and property insurance)

ARAG Lebensversicherungs-AG

(Life insurance)

ARAG Krankenversicherungs-AG

(Health insurance)

Interlloyd Versicherungs-AG

(Specialized in broker sales)

International companies

(Legal insurance/ legal services)

Service companies

ARAG IT GmbH

(IT services for the ARAG Group)

Cura Versicherungsvermittlung GmbH

(Brokerage firm)

ARAG Service Center GmbH

(Emergency telephone service)

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# Overview

## ARAG Holding SE Key Figures – Consolidated Financial Statements

(€ million)	2016	Change	2015	2014
<b>Sales revenue</b>				
Gross premiums written	1,729.7	4.4%	1,656.1	1,588.2
Premiums earned for own account	1,706.4	4.6%	1,631.2	1,567.6
Revenue of non-insurance companies	54.8	-17.7%	66.6	57.6
<b>Expenses</b>				
Claims incurred net of reinsurance	1,014.9	4.1%	974.6	985.9
Claims ratio (basis: premiums earned)	59.5%	-0.2% pts.	59.7%	62.9%
Own account insurance business operating expenses	546.5	3.0%	530.7	511.5
Cost ratio (basis: premiums earned)	32.0%	-0.5% pts.	32.6%	32.6%
<b>Net income overview</b>				
Underwriting result for own account	66.7	0.9%	66.1	60.6
Gains and losses on investments	240.0	13.7%	211.0	273.5
of which included in underwriting result	176.7	11.8%	158.0	201.0
Other net income/expense	-48.3	-15.3%	-57.0	-55.0
Profit/loss from ordinary activities	87.0	30.4%	66.7	84.5
Consolidated net income	43.1	47.6%	29.2	47.2
Technical provisions/ net premiums earned	349.6%	-1.2% pts.	350.8%	353.2%

# Profile of the ARAG Group

## Overview

The ARAG Group is the largest family enterprise in the German insurance industry and is one of the world's three leading providers of legal insurance. ARAG was established more than 80 years ago exclusively as a legal insurance company, but has now positioned itself as an international insurer of considerable renown offering innovative, high-quality insurance products. At the end of 2016, the Group sold ARAG Lebensversicherungs-AG as part of a strategic realignment to focus squarely on property and health insurance. The sale is subject to approval by BaFin. The Company aims to generate growth across all insurance segments in Germany and to exploit the potential for expansion in the international legal insurance business. Today, the ARAG Group operates in a total of 17 countries (Germany, 14 other European countries, the US, and – since 2016 – Canada) through branches, subsidiaries, and equity investments. It generates sales revenue and premiums of approximately €1.8 billion and employs more than 4,000 people.

ARAG SE is responsible for strategic Group management and the legal insurance operating business at both domestic and international levels. The other ARAG insurance and service companies are responsible for the operational management of their respective lines of business. ARAG Holding SE manages the assets and is the parent company of the Group from a company law perspective.

## Legal insurance

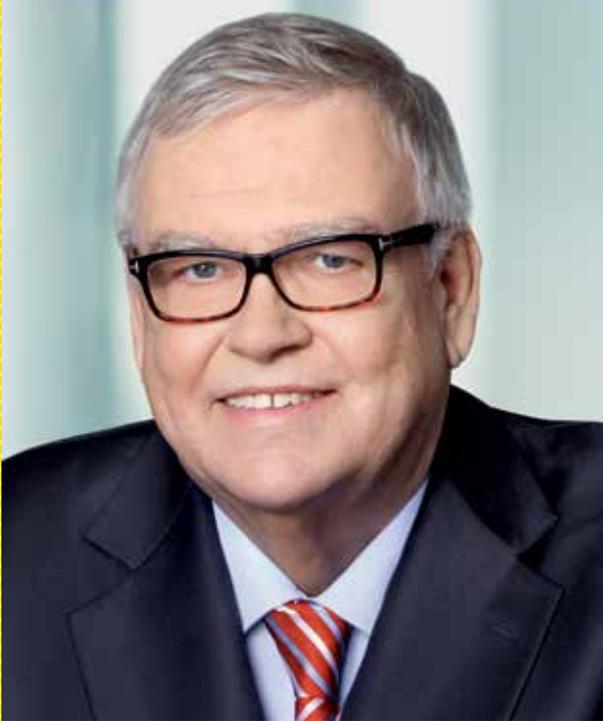
In its core legal insurance segment, ARAG plays a major role in shaping its markets both in Germany and abroad with innovative products and services. For some years now, the international legal insurance business has been the Group's most significant area of activity. The international units involved in this business are a valuable source of impetus for the Group's growth. At the same time, ARAG SE is following a clear path to success in its German domestic market, where it is generating rising legal insurance premiums.

## Casualty and property insurance

In a fiercely competitive market, ARAG Allgemeine is demonstrating its strength as an attractive provider of property, liability and accident insurance policies, which have been highly ranked in numerous independent performance comparisons. This company is also Europe's largest sports insurer, providing cover for over 20 million recreational sports participants and top-ranking athletes. ARAG Allgemeine's Interlloyd subsidiary specializes in brokering services in the commercial and private customer segments, adding a further dimension to the Group's portfolio.

## Personal insurance

In the private health insurance market, ARAG Kranken (ARAG Health) offers a broad range of highly efficient products, emphasizing its appeal as a provider of full-coverage and supplementary health insurance. To complement its range of products for customers, ARAG Core Sales successfully offers pension products from its strategic partner Alte Leipziger.



Dr. Dr. h. c. Paul-Otto Faßbender

## Introduction

The ARAG Group can look back on a very eventful and extremely successful year. Once again, the Company demonstrated its great capabilities – both in Germany and abroad. As in previous years, ARAG generated robust growth and increased its premium income by 4.4 percent in 2016. The huge amount of groundwork carried out in recent years is continuing to bear fruit. The Group continues to evolve at a rapid pace. We are winning new customers and continuing to grow our business while increasing our profitability.

ARAG's international business is in very good shape and is the Company's engine of growth. Premium growth of 7.6 percent was on a par with the strong performance of the previous year, with our activities in Spain, Italy, the Netherlands, and the US generating particularly substantial increases in premiums. The financial performance of our international business improved even more in 2016, having already been at a very good level.

In the very challenging German market, too, we achieved an exceptionally strong improvement in our key figures, including premium growth of 2.9 percent. This growth stemmed from property insurance, in particular from the German legal insurance business and from health insurance. As in 2015, this premium growth was accompanied by an expansion of the customer base in real terms. This is clear recognition from our customers of ARAG's good online service offering. Our online customer base now makes up 10 percent of the total customer base in Germany.

ARAG's earnings figures are encouraging, too: Profit from ordinary activities amounted to €87 million, a substantial year-on-year rise of 30 percent.

The ARAG Group's outstanding performance both in 2016 and in previous years emphasizes that the focus of our business on property and health insurance is increasingly proving to be a competitive advantage. For this reason and given the ongoing period of low interest rates, the Management Board and owners have decided to focus fully on these product areas. To this end, the shares in the life insurance segment will be sold to Frankfurter Leben-Gruppe – subject to approval from the German Federal Financial Supervisory Authority (BaFin).

ARAG's new structure will enable it to concentrate more on its proven strengths. The Group's ability to step up its property and health insurance business in Germany and to further internationalize its legal insurance business is the key to securing ARAG's future. In the years ahead, we will continue to show Drive, Pioneering Spirit, and Discipline as we take our Company forward for the benefit of our customers.



Dr. Dr. h. c. Paul-Otto Faßbender

## Group Management Report

### Changes in premium income and sales revenue

(€ million)	2016	2015	2014
<b>Legal insurance</b>	<b>893.0</b>	<b>841.7</b>	<b>787.2</b>
of which domestic	351.5	330.5	312.5
of which international	541.5	511.2	474.7
<b>Casualty and property insurance</b>	<b>266.1</b>	<b>246.6</b>	<b>238.8</b>
of which domestic	204.7	197.2	192.8
of which international	61.4	49.4	46.0
<b>Life insurance</b>	<b>213.7</b>	<b>220.3</b>	<b>221.6</b>
<b>Health insurance</b>	<b>356.9</b>	<b>347.5</b>	<b>340.5</b>
<b>Service companies</b>	<b>54.8</b>	<b>66.6</b>	<b>57.6</b>
<b>Total</b>	<b>1,784.5</b>	<b>1,722.7</b>	<b>1,645.7</b>

- ARAG remains on a steady path of growth with 4.4 percent more income
- German business expands by 2.9 percent
- Further significant rise in premiums in international markets of 7.6 percent
- Combined ratio falls to 91.5 percent
- Strong improvement in profit from ordinary activities

# Group Management Report

## I. Group Fundamentals

The ARAG Group is the largest family-managed insurance company in Germany and is one of the world's three leading providers of legal insurance. It focuses on state-of-the-art insurance products and services aimed at both private and small business customers. ARAG is a provider of high-quality insurance with a multidimensional approach, offering its customers in Germany not only its core legal insurance policies but also needs-based products and services in casualty and property insurance and personal insurance business. Against a backdrop of persistently low interest rates, ARAG SE began to reorganize the ARAG Group structure in 2016 and decided to sell its shares in ARAG Lebensversicherungs-AG to Frankfurter Leben-Gruppe. The sale of the shares is subject to approval by the German Federal Financial Supervisory Authority (BaFin).

ARAG began to make inroads into markets outside Germany more than 50 years ago. The main purpose was to set up separate international companies in the Group that could provide support for the German legal insurance customers in the event of a claim. It became clear that this model in itself was not sustainable. However, there was a demand for legal insurance within each of the countries themselves, as a result of which it was possible to develop new business models in line with the various circumstances and tap into new markets. Including Germany, ARAG now operates in a total of 17 European countries through branches, subsidiaries, and equity investments. The Company also launched business activities in Canada last year.

In addition to the Group headquarters in Düsseldorf and the personal insurance offices in Munich, the ARAG Group maintains, through ARAG SE, international branches in Austria, Belgium, Greece, Italy, the Netherlands, Portugal, Slovenia, and Spain. The international branches run their operating businesses in their national markets independently, taking into account the specific local circumstances in each case.

Legal insurance is also provided in the US, Norway, Sweden, and Denmark. In each case, the business is operated through legally independent affiliated companies, under the unified management of ARAG SE in its role as parent company. In addition, ARAG SE operates in Switzerland via an equity investment in a legal insurance associate. In the United Kingdom, a Group company acts as a broker for legal insurance business and legal-insurance-related special service package business, passing this business to four UK primary insurers. Some of this insurance is then ceded to ARAG SE under quota-share reinsurance treaties. This intermediary model has been adapted for use in the Canadian market.

ARAG SE also holds an equity investment in a legal insurance company in Luxembourg.

Building on its dynamic growth and great willingness to embrace change, ARAG is continuing to extend its competitive edge in property and health insurance. In doing so, it is continuing to take a systematic approach to internationalizing the legal insurance business.

## II. Report on Economic Position

### Economic and sector conditions

Global economic growth is currently only muted but, from a historical perspective, is not unusually slow. In fact, it appears to be returning to normal levels following the extreme expansion rates and related overheating in the run-up to the global financial crisis in 2008.

The turmoil in international financial markets at the start of 2016, the unexpected result of the Brexit referendum in the United Kingdom last summer, and the surprising outcome of the US presidential election have not had a lasting detrimental effect on the pace of global economic growth. Although the vote for Brexit and the new political regime in the US created heightened uncertainty in financial markets for a time, the impact on the real economy has been limited so far. Capacity utilization in manufacturing continued to increase. At the same time, the situation in emerging markets stabilized, above all thanks to the strengthening of the Chinese economy. The steadying of the oil price is also likely to have had a positive effect on commodity-exporting emerging markets.

Industrialized countries are going through a phase of economic recovery. In most of them, capacity underutilization in the product and labor markets decreased further in the first half of 2016. Particularly in the eurozone and Japan, economic output rose faster than the estimated potential output. By contrast, growth in the US was slightly lower than expected in the first half of the year. The German Council of Economic Experts currently estimates that total global production grew by 2.5 percent in 2016.

The eurozone's economic recovery continued over the course of 2016. Production in the economy as a whole has been rising steadily for three years now. Employment has risen noticeably in recent years; at 10.1 percent, the unemployment rate is at its lowest since 2011. The economic recovery is driven, above all, by domestic demand. In particular, there is steady growth in consumer demand. At the same time, the fall in the oil price has helped to push up real disposable income. The expansionary monetary policy of the European Central Bank (ECB) has also played a key part in the eurozone's economic growth. The proportion of government bonds with negative yields over the medium to long term has risen sharply. Purchase programs for government bonds and other securities have been hugely expanded in the past two years. Quantitative easing led to depreciation of the euro and a significant increase in prices of equities, real estate, and other assets.

The German economy also generated substantial growth in 2016. The German Council of Economic Experts predicted a 1.9 percent rise in real gross domestic product (GDP). Improved consumer sentiment reflected the good situation in the labor market. The number of people in employment is predicted to see a further rise of more than 500,000 to 43.6 million this year. Effective wages are also going up, albeit more slowly than in previous years. This year, household incomes have also benefited from the raising of the basic tax threshold and the tax threshold for parents and from repayment of some of the tax receipts caused by bracket creep. According to the German Insurance Association (GDV), growth in households' nominal disposable income will have been 2.7 percent in 2016. The rate of inflation, projected to be around 0.3 percent, was roughly the same as in 2015. The low inflation rate meant that the purchasing power of German households again rose significantly. Given the low interest rates, consumer spending also continued to be boosted by a relatively low propensity to save. The savings ratio for households will again go up slightly this year, although the increase of 0.8 percentage points since 2013 to its current level of 9.8 percent of disposable income is modest. Overall, the GDV expected an inflation-adjusted increase in household consumption of 2.0 percent in 2016.

Following the sharp rise in the capital market rate (yield on listed German government securities with a residual maturity of nine to ten years) during the summer, this rate fell back again to an average for the year of around 0.2 percent as a result of the rate of inflation remaining low last year. Share prices benefited from favorable macroeconomic conditions. Whereas the EURO STOXX 50's increase of 0.4 percent was only small, the German DAX share index climbed by 6.9 percent to 11,481 points at the end of the year.

The GDV's most recent forecasts for the insurance industry as a whole predicted that premium income would hold steady, barely changing compared with 2015, which had not seen any noticeable increase in premiums. By contrast, gross premiums written in direct casualty and property insurance business increased by 2.8 percent (projected). The reasons included increases in the sums insured and some extension of the cover in property insurance. In legal insurance, there was even stronger growth in premiums at around 5.0 percent owing to the opportunities to adjust premiums as part of cost increases resulting from Germany's Second Act Modernizing the Law on Court Costs (Second KostRMoG). Premium growth in health insurance was around 1.8 percent.

The property insurance segment had already taken a significant hit from the severe weather brought about by the low-pressure system Niklas back in 2015. In the year under review, it also had to deal with the adverse impact of heavy rain in some regions. According to GDV estimates, these extreme weather events between late May and early June 2016 gave rise to claims with a total value of €1.2 billion, substantially exceeding previous losses such as those caused by storm Ela in 2014. Nonetheless, as property insurers were spared any other major storms or hailstorms in 2016, it can be assumed that last year was slightly below average in terms of natural hazards. According to the GDV, a significant rise in the

number of claims made caused claims incurred in the legal insurance segment to increase further, which means that the combined ratio in this insurance segment is likely to be around 100 percent for 2016. Overall, the GDV predicted that the combined ratio for direct casualty and property insurance business would stagnate at 97.0 percent.

Life insurance continued to operate in tough conditions. This segment faces the difficult challenge of continuing to generate a guaranteed rate of return despite the persistently low interest rates. According to the GDV, the life insurance segment was likely to post a decline in premiums of 2.8 percent.

Private health insurance in Germany again held steady in 2016. The prolonged phase of low interest rates is continuing to affect gains and losses on investments. Overall, the segment registered premium growth of approximately 1.8 percent. With Bundestag elections due to be held in 2017, there is once again heated public and political debate about the issue of a citizens' health insurance scheme in Germany.

### **Business performance**

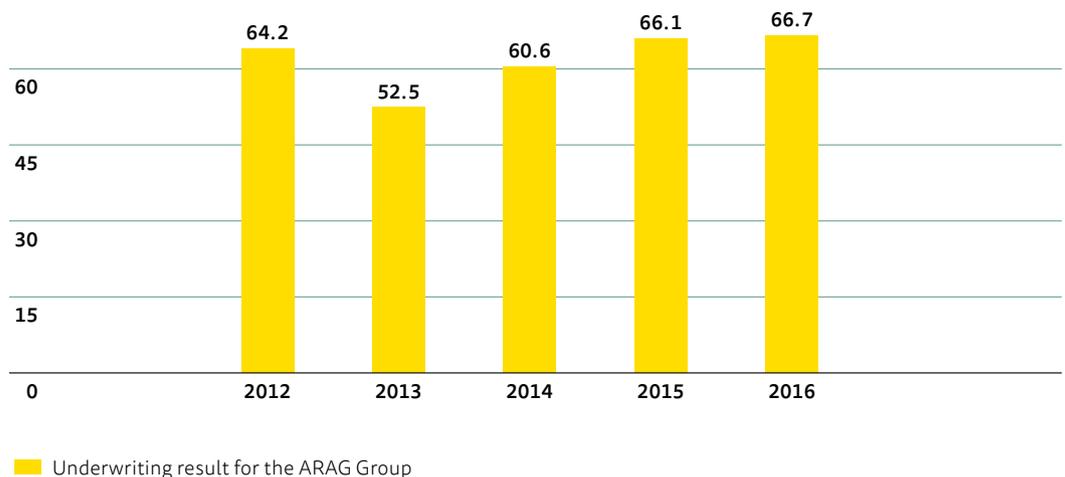
The ARAG Group's volume of business again expanded steadily and significantly in the year under review, with gross premium income advancing by 4.4 percent to €1,729.7 million. One of the main drivers of this increase was the strong growth in the legal insurance segment. In the German legal insurance market alone, gross premiums written from direct business rose by 6.6 percent year on year. International legal insurance business also provided considerable growth impetus, particularly as a result of the expansion of indirect business. Premiums in international business were up by 7.6 percent overall. The units reporting the strongest growth were those in Spain, Italy, the Netherlands, and the US. The casualty and property insurance segment in Germany and the health insurance segment, where premiums rose by 3.8 percent and 2.7 percent respectively, also made a significant contribution to growth. Against a backdrop of challenging conditions created by the sustained period of low interest rates, the life insurance business was – as expected – the only segment to register a decrease, with premiums falling by 3.0 percent in 2016.

As a result of the larger business volume, claims incurred in the legal insurance business as a whole increased from €426.8 million in 2015 to €440.0 million in the reporting year. Claims incurred in the casualty and property insurance business were also up, rising by €13.8 million. In life insurance, claims incurred grew to €233.1 million owing to policies expiring at the end of their term and due to increased surrender value payments. As expected, expenses for claims incurred in health insurance increased by a total of €9.0 million due to the ongoing expansion of this business. Overall, claims incurred by the Group in the year under review were up by 4.1 percent compared with the prior-year figure.

Insurance business operating expenses rose by 3.0 percent. This rise was attributable to the overall growth in the volume of business and the greater number of employees, particularly in the international branches and subsidiaries. The cost increases were contained as a result of the statutory discount rate for provisions for pensions and other post-employment benefits being raised from a seven-year to a ten-year average. This resulted in a one-off decrease in pension and other post-employment benefit expenses during the reporting year. Insurance business operating expenses increased to €546.5 million (2015: €530.7 million). Nevertheless, the cost ratio fell slightly in 2016, from 32.6 percent to 32.0 percent, because of the greater volume of business.

### Changes in underwriting result

(€ million)



The ARAG Group's underwriting result rose slightly, advancing from a profit of €66.1 million in 2015 to €66.7 million in 2016. The decrease registered with respect to the personal insurance policies was easily offset by the substantial improvement in the underwriting result reported for the property insurance business.

There was a very significant increase in the underwriting profit in the legal insurance segment, whereas the casualty and property insurance business's underwriting result declined considerably. The life insurance business reported an underwriting loss.

Despite the impact of the protracted phase of low interest rates, the net gains on investments increased further. Reversals of write-downs went up again whereas write-downs were lower than in 2015. On the other hand, ordinary income from investments declined, as expected. Overall however, the net gains on investments – where not assigned to the underwriting result – increased significantly year on year, rising from €54.0 million to €64.0 million.

Other net income/expense amounted to a net expense of €48.3 million, which was lower than the equivalent figure of €57.0 million in 2015, as expected. The main reason for this was the one-off reduction in pension and other post-employment benefit expenses resulting from the changed discount rate for defined benefit obligations.

At €87.0 million, profit from ordinary activities was again at a very good level (2015: €66.7 million).

The net extraordinary expense of €0.3 million (2015: net expense of €0.3 million) arose in connection with expenses from the application of the transitional provisions in the Introductory Act to the German Commercial Code (EGHGB) relating to the accounting treatment of pension and other post-employment benefit obligations.

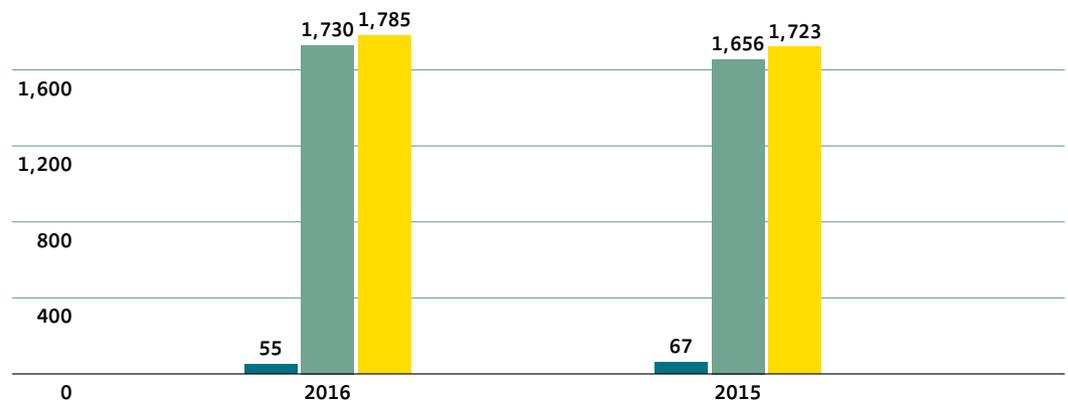
Consolidated net income amounting to €43.1 million was impacted by write-downs on the net deferred tax assets in Germany of €24.7 million.

**Premiums/sales revenue** The 4.4 percent rise in the premium income of the insurance companies in the ARAG Group reflects their consistently strong business performance in recent years. As described above, all national and international ARAG units except the life insurance business provided encouraging growth impetus for the Group.

Even though growth in the overall German insurance market was slight at just 0.2 percent, the ARAG Group raised its premium income by an above-average 2.9 percent despite the tough environment. Premium income in Germany amounted to €1.13 billion compared with €1.10 billion in 2015. In the German legal insurance business (including inward reinsurance business), premiums rose by €20.9 million to €351.5 million. The German casualty and property insurance business grew by €7.4 million to €204.7 million. Health insurance business went up by €9.4 million to €356.9 million, whereas life insurance premiums fell by €6.6 million to €213.7 million. Sales revenue generated by the Group's service companies decreased by €11.8 million to €54.8 million. Total premium income and sales revenue in the ARAG Group advanced by 3.6 percent, from €1.72 billion in 2015 to €1.78 billion in the year under review.

### Gross revenue for the period

(€ million)

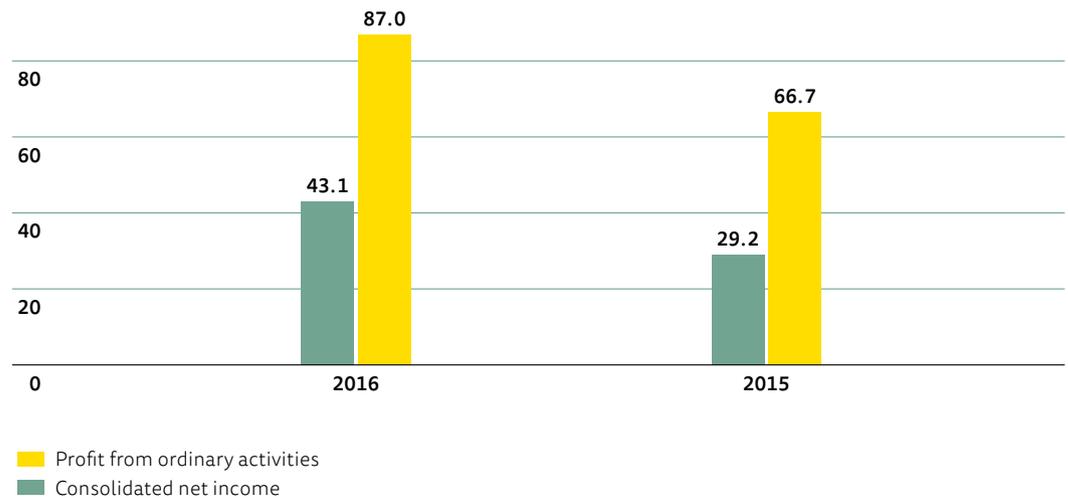


- Gross revenue for the period for the ARAG Group
- Insurance company premiums
- Service company sales revenue

The Group's portfolios comprised 7.1 million policies (December 31, 2015: 6.6 million). Of this total, 3.5 million policies (December 31, 2015: 3.1 million) were attributable to international business. Added to this were a further 20.8 million insured risks in the domestic sports insurance business (property and casualty insurance segment), which were covered via group policies with 18 state sports associations.

### Net income

(€ million)



### Financial performance

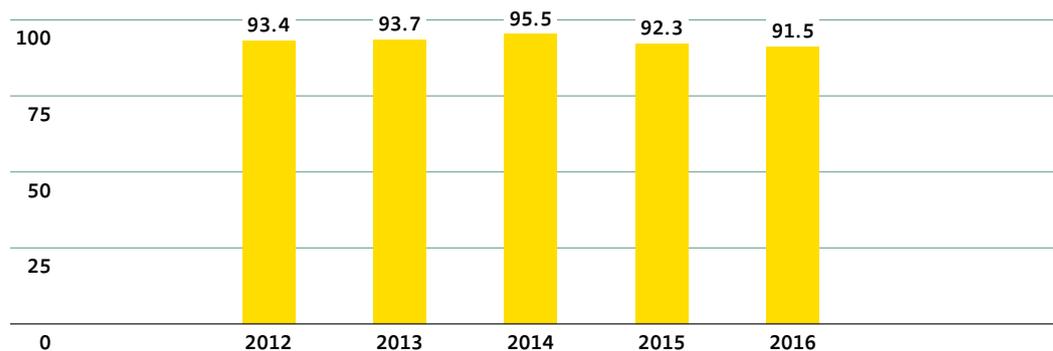
ARAG again highlighted its significant earnings power in the year under review. In the segments, the underwriting result and volatility in capital markets mostly offset each other. Moreover, a further fall in interest rates resulted in the reversal of write-downs of institutional fund shares/units. Overall, the ARAG Group was able – due in part to the slight improvement in its underwriting result – to raise its financial performance significantly compared with 2015.

The underwriting result, which was boosted by a 4.6 percent rise in net premiums earned, came to €66.7 million (2015: €66.1 million). The main reasons why the increase in the underwriting result was not higher were the €40.3 million growth in claims incurred and the €15.7 million rise in insurance business operating expenses. Expenses for claims incurred advanced from €974.6 million to €1,014.9 million, a year-on-year increase of 4.1 percent. Nonetheless, the Group claims ratio improved slightly, falling from 59.7 percent to 59.5 percent. The Group cost ratio also went down slightly in 2016, dropping from 32.5 percent to 32.0 percent.

The Group was able to reduce its combined ratio from 92.3 percent in the previous year to 91.5 percent.

## Changes in combined ratio

(%)



■ Combined ratio for the ARAG Group

The increase in the net gains on investments from €54.0 million to €64.0 million arose primarily as a consequence of higher interest-rate-related reversals of write-downs on securities in 2016 and higher write-downs in 2015 combining to offset the decrease in ordinary income.

Other net income/expense received a substantial boost from the change to the statutory discount rate for pension and other post-employment benefit obligations. Accordingly, the net expense declined from €57.0 million to €48.3 million.

Profit from ordinary activities improved significantly: The figure of €87.0 million was the highest level seen in the past four years and represented a year-on-year rise of 30.4 percent (2015: €66.7 million).

Extraordinary expenses of €0.3 million arose from the revaluation of pension provisions and pre-retirement part-time working obligations in application of the transitional provisions under the German Accounting Law Modernization Act (BilMoG).

Overall, profit before tax and before non-controlling interests advanced from €66.5 million in 2015 to €86.8 million in 2016.

The consolidated tax expense, which was adversely affected by the write-downs on net deferred tax assets of €24.7 million, amounted to €43.7 million (2015: €37.2 million). After deduction of taxes and non-controlling interests, consolidated net income was up by 46.3 percent compared with 2015 and came to €42.8 million.

## Financial position

The objective of the management of financial resources is to ensure that the Company holds adequate capital and manages its liquidity such that it is able to satisfy its obligations arising from the insurance business at all times and to exceed, rather than simply satisfy, the regulatory requirements concerning the solvency capital adequacy of insurance entities. The subordinated liabilities reported on the balance sheet qualify as basic own funds in accordance with section 89 (3) no. 2 of the German Insurance Supervision Act (VAG). These subordinated liabilities comprise a registered bond with a value of €30.0 million that matures on July 29, 2024.

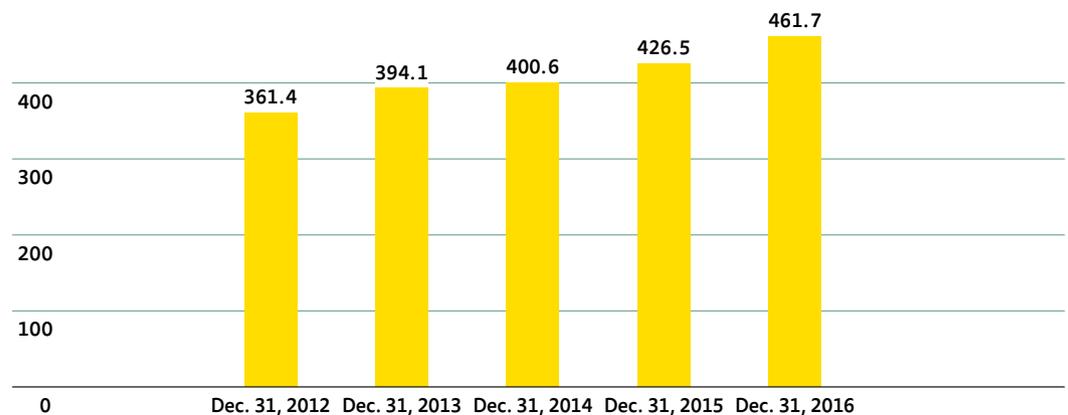
The underwriting liabilities are covered by investments of €6,483.6 million (December 31, 2015: €6,123.3 million). In addition to current bank balances and cash on hand of €195.6 million (December 31, 2015: €155.3 million), the ARAG Group has investments at its disposal that can be sold on the capital and financial markets at short notice, thus ensuring that the Group is able to satisfy its payment obligations under insurance contracts at all times.

The Group's equity rose from €426.5 million to €461.7 million as of December 31, 2016.

Further information on the extent of investments, purchases of intangible assets, and changes in the liquidity of the Group in the year under review can be found in the cash flow statement on page 95.

## Changes in equity

(€ million)



■ Consolidated equity

### Net assets

The Group's portfolio of investments swelled by 5.9 percent in 2016, from €6,123.2 million to €6,483.6 million. The fair value of these investments amounted to €7,259.1 million as of the balance sheet date (December 31, 2015: €6,814.1 million).

The breakdown and year-on-year changes in investments were as follows:

### Type of investment

(€ million)		Dec. 31, 2016		Dec. 31, 2015	
I.	Land and buildings	237.1	3.7 %	243.2	4.0 %
II.	Shares in affiliated companies and equity investments	20.5	0.3 %	35.5	0.6 %
III.	Lending to affiliated companies and equity investments	0.0	0.0 %	0.2	0.0 %
IV.	Equities and investment fund shares/units	2,432.2	37.5 %	2,330.5	38.1 %
V.	Bearer bonds	1,642.8	25.3 %	1,428.0	23.3 %
VI.	Loans secured by mortgages and land charges	88.8	1.4 %	114.1	1.9 %
VII.	Registered bonds, promissory notes	1,729.3	26.7 %	1,701.2	27.8 %
VIII.	Bank deposits	195.6	3.0 %	155.1	2.5 %
IX.	Sundry lending	6.8	0.1 %	4.4	0.1 %
X.	Miscellaneous investments	86.1	1.3 %	74.9	1.2 %
XI.	Deposits with ceding insurers	44.4	0.7 %	36.1	0.6 %
<b>Total</b>		<b>6,483.6</b>	<b>100.0 %</b>	<b>6,123.2</b>	<b>100.0 %</b>

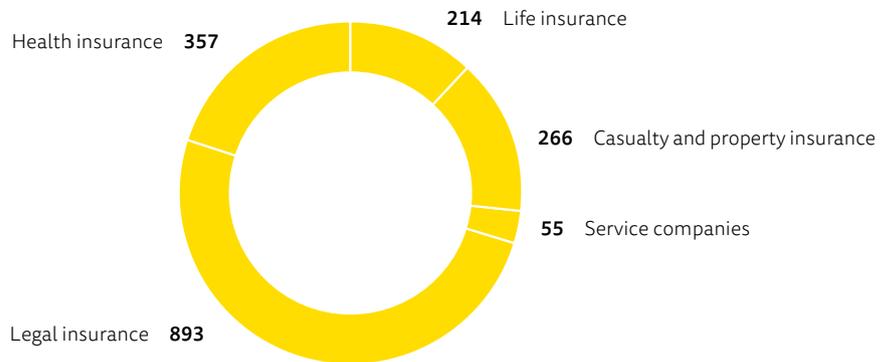
### Segment reporting

The Group comprises the following operating segments:

- Legal insurance
- Casualty and property insurance
- Health insurance
- Life insurance
- Services and asset management.

### Premiums and sales revenue by segment in 2016

(€ million)



### Gross premium income

(€ million)	2016	2015
Legal insurance	893	842

### Legal insurance

In 2016, the legal insurance segment underlined its important role as the fastest-growing and most profitable insurance segment in the ARAG Group. A further strong increase in Germany, along with the continuation of the growth trajectory in international markets, resulted in overall growth of €51.3 million. ARAG registered the greatest growth impetus in Spain, Italy, the Netherlands, and the US.

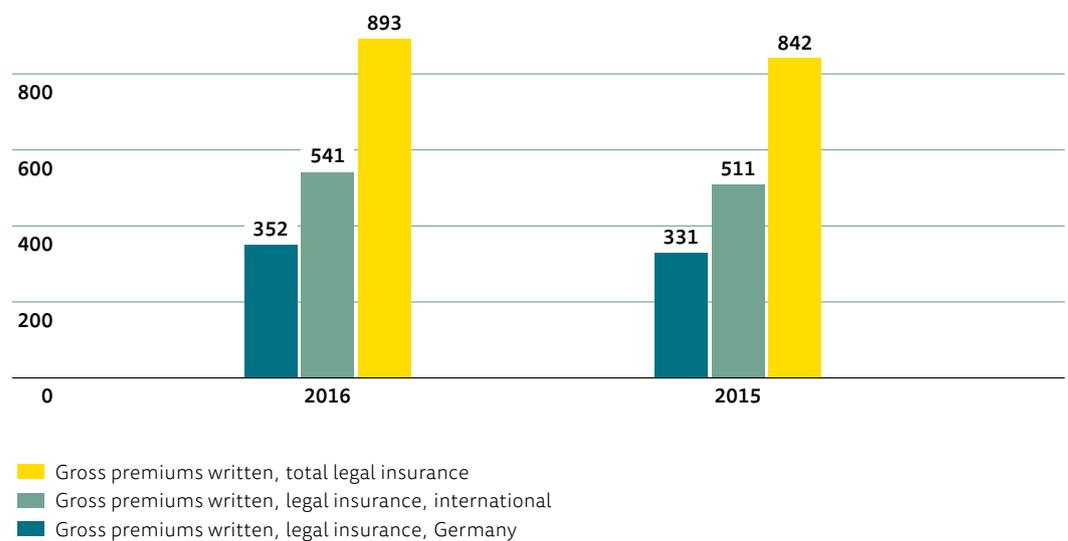
From an already high prior-year level, the segment's gross premiums written again rose substantially, advancing by 6.1 percent to €893 million in the year under review (2015: €842 million). At 60.6 percent, the share of total legal insurance premiums attributable to international legal insurance business was on a par with the previous year (2015: 60.7 percent).

Expenses for claims incurred in the whole of the legal insurance segment rose from €426.8 million to €440.0 million. The main contributing factors are explained in the following disclosures on the German and international legal insurance business. Overall, the segment's claims ratio went down from 51.4 percent to 49.5 percent. Despite the increase in the number of employees as planned, the cost ratio dropped from 44.2 percent to 43.2 percent because of the one-off reduction in pension and other post-employment benefit expenses. The underwriting profit for the entire legal insurance segment rose significantly in 2016, by €27.2 million to €63.5 million.

Net gains on investments in the legal insurance segment were virtually unchanged on their prior-year level at €74.9 million (2015: €74.6 million). The segment generated profit from ordinary activities of €103.7 million (2015: €69.7 million). This included the other net income/expense, which came to a net expense of €34.7 million – a significant year-on-year improvement (2015: net expense of €41.1 million) that was primarily due to lower pension and other post-employment benefit obligations.

### International legal insurance business shows continuous growth

(€ million)



The year under review saw further growth in the **international legal insurance business**. The ARAG Group provides products and services for customers in Germany and a total of 16 other countries. The largest international ARAG business units operate in the Netherlands, Spain, Italy, and the US.

Income from gross premiums written in the international legal insurance business rose by 6.0 percent year on year (2015: 7.7 percent), from €511.2 million to €541.6 million.

ARAG's long-standing, major international activities stood out for their strong performance last year. Business increased by €16.5 million in Spain, by €12 million in Italy, by €7.6 million in the US, and by €6.6 million in the Netherlands.

Additional premium income of €60.9 million (2015: €48.9 million) was derived from the legal-insurance-related special service package business generated by the Spanish, Italian, and Portuguese branches of ARAG SE, which is seeing especially buoyant growth. These premiums are reported under the casualty and property insurance segment.

In the reporting year, the expenses for claims incurred in the international legal insurance business climbed from €217.2 million to €227.5 million due to the considerably larger business volume. Overall, the claims ratio fell to 42.0 percent (2015: 43.1 percent). As a consequence of the effects described above, the combined ratio in the international legal insurance business improved from 88.1 percent to 86.7 percent.

The **German legal insurance business** maintained its path of growth. Once again, the rise in premium income of 6.3 percent outstripped the market average. But ARAG not only increased its premiums, it also achieved effective growth in its customer base. The robust expansion of new business is accompanied by a continued decline in policy cancellations. Taking account of the slower rise in inward reinsurance business as a result of movements in the euro/pound sterling exchange rate, the total income from gross premiums written in German legal insurance business amounted to €351.5 million (2015: €330.5 million).

The claims ratio in the German legal insurance business went down from 64.2 percent in 2015 to 61.3 percent in 2016. By contrast, the absolute amount of claims incurred rose from €209.6 million in the previous year to €212.6 million because of the larger volume of business. This amount includes additional provisions recognized for cumulative claims that could arise in connection with the emissions issue affecting VW diesel vehicles.

The net cost ratio fell sharply to 40.7 percent in 2016 (2015: 43.0 percent). This reduction was due to the strong growth in premiums and the aforementioned favorable changes to provisions for pensions and other post-employment benefits. The absolute year-on-year rise in insurance business operating expenses therefore totaled only €0.4 million.

An amount of €0.4 million was added to the equalization provision for the inward reinsurance business (2015: €0.2 million).

Overall, the underwriting loss generated by the German legal insurance business improved significantly year on year, falling to €6.0 million (2015: €22.4 million).

### Casualty and property insurance

ARAG's very good business performance in property insurance was reflected in the casualty and property insurance segment. Gross premiums written rose by 7.9 percent to €266.1 million in the year under review (2015: €246.6 million). The product portfolio, which has been significantly modernized, is attracting a great deal of interest from customers, leading to expansion of business in the general accident insurance, general liability insurance, composite residential buildings insurance, and home contents insurance divisions. Sales through brokers via the Group's own brokerage specialist, Interlloyd Versicherungs-AG, also contributed to the increase in premiums with growth of 4.6 percent. Premium income from the legal-insurance-related special service package business in the Spanish, Portuguese, and Italian branches of ARAG SE is allocated to the casualty and property insurance segment.

As described in the section on economic and sector conditions, one of the factors with a negative impact on the insurance industry's level of claims incurred last year was heavy rain. However, ARAG Allgemeine remained largely unaffected by these regional extreme weather phenomena in 2016. Overall, the claims reported for 2016 were down by more than 4 percent year on year. However, this was more than offset by the greater need for provisions for claims incurred but not reported (IBNR claims) and for benefit reserves for annuities. The increase in ARAG SE's in-force legal-insurance-related business through branches in Spain, Portugal, and Italy caused claims incurred to rise by an additional

Gross premium income		
(€ million)	2016	2015
Casualty and property insurance	266	247

€4.5 million. Expenses for claims incurred in the property and casualty segment totaled €138.9 million and were thus higher than the prior-year level of €125.1 million. Despite the good premium growth, the claims ratio increased from 52.5 percent to 54.8 percent.

The cost ratio was unchanged year on year at 40.2 percent. Underwriting profit before the equalization provision fell from €16.8 million in 2015 to €12.4 million in the reporting year. After an addition to the equalization provision of €9.9 million, the underwriting profit amounted to €2.5 million (2015: €12.5 million). Profit from ordinary activities in the casualty and property insurance segment amounted to €11.4 million (2015: €16.5 million), which included a year-on-year improvement of €1.4 million in net gains on investments and a reduction of €3.5 million in other net expense.

### Gross premium income

(€ million)	2016	2015
Health insurance	357	347

### Health insurance

As in previous years, premium income in the health insurance business grew at a faster rate than in the market as a whole. Gross premium income advanced by 2.8 percent to €356.9 million (2015: €347.5 million), whereas the market registered growth of 1.8 percent. The increase in premiums was predominantly attributable to the rise in new business. Premium adjustments were modest compared with the rest of the market. The solid growth generated by the health insurance business underlined its strategically important role as ARAG's largest area of business in the German market.

In addition to the traditionally rapidly expanding supplementary health insurance business, full-coverage insurance was one of the main drivers of growth in the reporting year.

On the benefit expenses side of the equation, higher expenses for claims incurred and the addition to the actuarial reserve, which was up by 16.4 percent year on year, totaled €343.7 million compared with €314.9 million in 2015.

The underwriting result declined accordingly in the year under review, falling from a profit of €14.5 million in 2015 to €8.5 million in 2016. The net gains on investments included in this figure rose by €17.1 million year on year to €67.5 million.

After taking into account the sundry income and expense items and the addition to the provision for bonuses and rebates, profit before tax decreased to €6.8 million (2015: €11.1 million) but was nevertheless once again higher than the budgeted figure.

### Gross premium income

(€ million)	2016	2015
Life insurance	214	220

### Life insurance

ARAG made significant changes in preparation for the future in its life insurance business last year. In view of the protracted phase of low interest rates, ARAG SE – the Operating Group Holding Company – decided to reorganize the structure of the ARAG Group. ARAG SE then initiated the sale of its shares in ARAG Lebensversicherungs-AG to Frankfurter Leben-Gruppe. The sale is subject to approval by the German Federal Financial Supervisory Authority (BaFin).

As anticipated, the announcement of this decision caused a further reduction in new business on top of the noticeable decline triggered by adjustments to the remuneration system to meet the requirements of the German Life Insurance Reform Act (LVRG). Total premiums in new business fell by 16 percent year on year to €338.8 million. Accordingly, gross premiums written decreased from €220.3 million in 2015 to €213.7 million in the year under review.

On the benefit expenses side, expenses for claims incurred and the change in the actuarial reserve amounted to €279.0 million, a year-on-year decline of €1.3 million. Front-end fees fell by 21.0 percent in 2016 to €17.4 million. At €7.2 million, administrative expenses were down slightly compared with the previous year (2015: €7.6 million). Gains and losses on investments assigned to the underwriting account amounted to net gains of €111.5 million (2015: €109.8 million). This year-on-year improvement of €1.7 million was due to higher reversals of write-downs and only small write-downs on institutional funds. After taking into account the sundry income and expense items as well as the tax position, the segment generated a profit before the provision for bonuses and rebates of €2.6 million (2015: €4.2 million). This amount was allocated in full to the provision for bonuses and rebates (2015: €4.2 million). For the purposes of determining the consolidated net profit for the year, the loss before tax amounted to €8.9 million compared with a profit of €2.9 million in 2015.

### Services and asset management

This segment brings together those Group companies that provide core services outside straightforward insurance business or operate non-insurance business, such as IT services, the central emergency telephone service for ARAG customers, and the real estate development business for third parties. The segment also consists of the holding companies, including ARAG Holding SE. The insurance brokerage firm in the Group, Cura Versicherungsvermittlung GmbH, and the insurance agent for the UK reinsurance business are also assigned to this segment. The real estate development business was sold at the end of the third quarter. The sales revenue generated by the non-insurance companies with third parties and the other segments in the Group therefore fell from €108.5 million in 2015 to €98.0 million in 2016. After adjustment for the intragroup sales revenue in the service companies, the remaining sales revenue generated from third parties came to €54.8 million compared with €66.6 million in 2015. Profit before tax was €29.3 million (2015: €32.7 million).

### Consolidation

Transactions between the Group's segments are offset in order to present the Group as one overall entity. Business between Group companies that are allocated to the same segment is consolidated when the segment reporting is produced so as to present each segment as one unit.

Transfers between segments are largely the result of the receipt of dividends in the multilayer Group structure. Intercompany charges for services between group companies are also eliminated.

### Sales revenue

(€ million)	2016	2015
Service companies	55	67

### **Sales organization**

The Group's sales organization makes a fundamental contribution to ARAG's business success in Germany. ARAG Core Sales is the traditionally strong sales channel selling ARAG products exclusively: The 1,000-plus ARAG Sales Partners use the network of over 160 main branch offices and other branch offices across Germany to provide customers with professional, face-to-face support and advice at local level. This is underpinned by ARAG's holistic 'Red Thread' approach to insurance advice and support. For customer visits, ARAG Sales Partners can use either a paper version or a digital version for tablets that can be accessed via a proprietary advice app. Core Sales also uses digital touchpoints for greater connectivity, whether for contact with customers or to sign up new sales partners. Use of the holistic 'Red Thread' approach to insurance advice is an integral element of the basic training delivered by the ARAG sales academy, whose broad-based and regularly updated range of courses ensure the exclusive agents receive high-quality training and development on ARAG and its products.

ARAG Partner Sales is ARAG's successful sales channel specializing in brokers and non-exclusive agents. It has a wealth of experience in working with a wide variety of target groups, from specialist brokers to pool structures and sales outfits. Streamlined structures and processes minimize the effort involved for agents, while knowledgeable contacts in the Field Sales and Sales Administration organizations ensure that brokers and non-exclusive agents receive professional support in every regard. The online portal for brokers was completely revamped in 2016 and, besides being easier to use, includes plenty of useful new content.

In the year under review, the two main sales channels in Germany accounted for 42.8 percent (Core Sales) and 33.1 percent (Partner Sales) of new policies underwritten. Following the growth in 2015, ARAG saw a further increase in its customer base for online business to more than 200,000 customers in 2016. This equates to almost 10 percent of the German customer base. The online business is thus developing into a relevant sales channel with which ARAG can reach out to internet-savvy customer groups. In Germany, the ARAG sales channel mix also includes sales partnerships in which made-to-measure, high-performance ARAG insurance solutions are sold under partnership agreements with other insurance companies, banks, other companies, associations, and clubs.

### **Non-financial performance indicators**

The ARAG Group has set out its self-image very clearly in its corporate guidelines: ARAG is the internationally successful, innovative quality insurer – independent and family-owned. For more than 80 years, the business concept has been based on the aim of establishing equality of opportunity. Accordingly the ARAG Group helps its customers create scope to make personal choices – at all stages of their lives. Based on innovative insurance products and beneficial services, ARAG minimizes the risks faced by its customers, so that customers can concentrate entirely on the opportunities available to them, leading an active, independent life. This is also clearly reflected in the brand tagline 'ARAG. Dive into Life'.

ARAG again added a wide range of content to the section with the same title on its website [www.ARAG.de](http://www.ARAG.de) in 2016. It also ran new and attractive adverts as part of the successful advertising campaign launched in 2015. The aim is to demonstrate the day-to-day relevance of ARAG products and services. The brand promotion film, which was shown on TV and in movie theaters throughout Germany before selected movies likely to reach a wide audience, complemented three online commercials featuring ARAG product innovations. A radio commercial was added to the Germany-wide campaign in the autumn.

Another major, and logical, step taken in 2016 was the modernization of ARAG's logo. The family enterprise is thus reflecting the lasting changes that have taken place in recent years. The new ARAG logo, which had last been updated 13 years ago, was launched at the end of March 2016 at the same time as the new campaign. The word ARAG is a lot more prominent and easier to read, and the crossed swords have been removed. This new and modernized logo is thus more suited to the broad product portfolio of ARAG, which today offers appealing legal insurance products in Germany and 16 other countries and is also a successful provider of attractive health insurance and casualty and property insurance.

In the year under review, the ARAG Group again systematically expanded its products and services – always clearly guided by the constantly changing requirements and needs of customers and consumers. Based on optimum integration between these innovative product activities, a highly efficient workforce, a state-of-the-art brand presence, and clear strategic positioning as an independent, international provider of high-quality insurance products and services, ARAG has established the best possible foundations for further sustainable growth.

**Innovation** Innovativeness is a key driving force for ARAG and one of its major strengths. Besides refining the portfolio, the Company has implemented new and groundbreaking ideas for products and services that are always geared to meeting customer requirements and creating benefits for them. Four accolades awarded in 2016 are external recognition of the Group's ability to innovate: At the Plus X Awards, the Premium variants of ARAG's legal insurance, personal liability insurance, and accident insurance each won the Most Innovative Brand Award in 2016 in the insurance category. ARAG's new Sofort legal insurance product for motorists won a Golden Bull award (third place) in the Insurance Innovation of 2016 category. This is the third time that ARAG's legal insurance products have been among the winners in this competition run by the *€uro* and *€uro am Sonntag* magazines: ARAG *web@ktiv* online legal insurance was a prizewinner in 2013 and ARAG *Aktiv Immobilie* premium legal insurance for real estate was a prizewinner in 2015.

ARAG's Sofort legal insurance for motorists, which is unlike any other product available in the market, represents a new approach for the Group. For the first time, cover is provided for legal insurance claims incurred before the policy was taken out. This applies to administrative offenses and to claims for damages following a road accident. Since launching the product, ARAG has already provided immediate assistance in several

hundred cases even though the insurance policy was not in place at the time the claim was incurred. Feedback has been very positive. Besides this retroactive insurance, customers have also benefited from the three-year period (starting on the first day the policy is taken out) of the extensive benefits provided with the Komfort variant of ARAG legal insurance for motorists, including legal insurance in matters of contract law, property law, criminal law, administrative law, and tax law.

In the reporting year, the ARAG Group also demonstrated its pioneering role in the market with its unique range of services, such as telephone advice on conflict resolution and mediation services that can be purchased individually at a fixed price. Since mid-2016, it has been possible to book expert support from an experienced mediator directly at [www.ARAG-streitschlichter.de](http://www.ARAG-streitschlichter.de), whether for family arguments, disputes with an employer, contractual problems, or conflicts with authorities. The service is provided by mediators at the subsidiary ARAG Service Center GmbH (ASC).

ARAG Allgemeine, the provider of casualty and property insurance in the ARAG Group, went to market in 2016 with ARAG Alltagshelfer®, an innovative and flexible insurance product for individuals that offers support in the form of various assistance services for when unforeseen events disrupt everyday life. Since the first half of 2017, ARAG Business Assistance has also been available, providing a package of services suitable for the self-employed and small businesses as part of a self-contained policy. The package includes preventive measures and training on the prevention of loss/damage and for the benefit of the business, legal-insurance-related services such as receivables management and online contract verification, support such as finding a tradesperson to deal with burst pipes or electrical damage, cover for the cost of returning home in the event of significant damage to the office while travelling, as well as additional services such as arranging for replacement equipment.

In the reporting year, the ARAG Group again impressed customers with a variety of digital innovations. As well as continuously expanding the existing live chat function, which is heavily used by customers as an alternative means of communication, the Group introduced a number of new features. These include alternative methods of payment, with which ARAG entered uncharted territory for the insurance industry last year: Since May 2016, customers have also been able to pay recurring insurance premiums by credit card or PayPal for the first time. This new feature was first introduced for private legal insurance products that can be taken out online.

In autumn 2016, ARAG became the first insurance company in the market to offer a digital service card. Available for legal insurance and casualty and property insurance customers, the ARAG Wallet-Card can be installed on a smartphone, so customers can access all their important data, such as their policy number or the contact details for headquarters and their advisor, while on the go. Telephone numbers can be dialed and emails and websites opened directly from the app. Since the end of 2016, legal insurance and casualty and property insurance customers have also had their policy number sent to them in a text message when they take out the policy; they also receive a link that enables them to install the ARAG Wallet-Card easily and directly.

There were also a number of innovations for the sales partners of ARAG Core Sales in the year under review. Many new features were added to the advice app that had been launched in 2015, including navigating to the customer, downloading sent advisory docu-

ments, transmitting appointments and contacts via QR code, scanning policy numbers using the camera, recording spoken notes, using digital signatures, and selling legal insurance directly from the app. Not only the branch offices but also all individual partners of ARAG Core Sales now receive a complete ARAG-branded website with all the functions, including simple page navigation with clear product information, that has been optimized for use on tablets and smartphones. Policies taken out online via sales partners' websites are allocated directly to the respective partner.

ARAG's website has also been optimized at international level and standardized in order to strengthen the brand. This included establishing a central online platform for European countries that is progressively being rolled out to them. It features a standardized content management system with an identical navigation concept. The system can be maintained in the relevant local language, and its responsive design ensures that page content is automatically presented in an optimum manner for the various end devices, including smartphones and tablets. An integrated analysis tool collects details of the usage behavior of visitors and customers, thus enabling the website to be adapted and optimized specifically for users in each country.

**Products** As an innovative provider of high-quality insurance, the ARAG Group does more than simply launch brand new and innovative product concepts. It also constantly refines its existing broad range of products and services for the German and international markets in order to ensure the products and services meet the needs of prospective and existing customers.

Last year, for example, many new types of legal insurance were introduced. ARAG's unemployment protection product protects private customers against financial loss if they become unemployed through no fault of their own as a result of compulsory redundancy. The special employment legal insurance for seniors covers employment that supplements a pension. It also includes legal advice insurance and insurance for people with domestic employees.

A particular highlight of 2016 for self-employed people and small business owners was the addition of Receivables Management Plus to ARAG Aktiv-Rechtsschutz Premium legal insurance for the self-employed. The new feature offers the advantages of business agreement legal insurance combined with online receivables management. In addition, the ARAG JuraCheck® legal advice service has been expanded and is now always included in the premium variants of legal insurance policies for private and small business customers, who receive help from specialist attorneys when having employment contracts and references checked. These attorneys can also answer questions about contracts and check the legal aspects of customers' own websites. ARAG legal insurance is now available for price-conscious private customers and the self-employed in two additional Flex variants with different deductibles, enabling customers to decide on a case-by-case basis whether they want to hire their own attorney or – in return for a lower deductible – call on an attorney from ARAG's network.

The high quality of ARAG's legal insurance products can be seen from the many accolades and ratings. In 2016, for example, these included certification of ARAG Aktiv-Rechtsschutz legal insurance for the self-employed by the TÜV product standards regulator in Saarland – with excellent results: The Premium and Komfort packages were rated 'very good', the Basic variant was rated 'good'. And in a test of legal insurance products carried out by insurance IT specialists Softfair, the Flex variant of ARAG's new premium legal insurance range, launched in 2016, was rated 'excellent' three times – for the Family, the Senior, and the Singles packages.

ARAG SE was also a trailblazer outside Germany in 2016. The Dutch branch, for example, expanded Flexpolis, a bespoke private legal insurance product sold through Noordhollandse Versicherung. The product, for which customers choose the modules they need, now comes with several additional inclusive benefits. In the Italian market, ARAG Italy launched a new version of its private legal insurance product for families. A modular structure is also the distinctive feature of this product, with a wide range of optional modules and various levels of deductibles available depending on whether the customer chooses to use ARAG's network of attorneys. The Spanish branch has also brought in various new online services for its customers. These include special web protection (including software) for parents of minors as well as CyberSchutz for problems on the internet that offers customers a deletion service for unwanted online content and provides legal assistance to help stop cyberbullying. New services have also been added specifically for online shopping – including the drafting and verification of sales contracts – and for the preparation of wills. In 2016, ARAG Austria developed a new commercial legal insurance product for start-ups and launched it on the market at the beginning of 2017. ARAG Slovenia introduced legal insurance for property managers that can be taken out in conjunction with fire insurance from a strategic partner.

In the Norwegian market, the ARAG subsidiary HELP Forsikring AS expanded its range of legal insurance products for small and medium-sized enterprises: The product, which was launched in the previous year, is now also available to companies with more than 20 employees through group policies with Norwegian labor unions. The HELP Försäkring branch in Sweden has also added to its portfolio, developing and launching My Safety to provide cover for identity theft. The newly established ARAG Services Corporation, which acts as a broker in the Canadian market, has developed new private and commercial legal insurance products and entered into its first strategic alliances. It also provides its customers with a document center, which is a database containing a variety of legal documents that are available for download.

ARAG Allgemeine, which provides casualty and property insurance, also introduced further targeted updates for its insurance portfolio. It launched ARAG Alltagshelfer® in 2016, the first service product of its kind in the market. The new product provides help with many practical and organizational tasks that have to be carried out when everyday life is affected by events such as a hospital stay, birth or death in the family, or even strikes organized by a labor union. Customers receive all kinds of assistance and care services

when they need emotional and practical support in exceptional circumstances such as these, including laundry and meal services, shopping, house cleaning, childcare and pet sitting, and psychological counselling over the telephone.

At the beginning of 2016, the premium ARAG 'Recht&Heim' all-round cover package was upgraded to include extensive benefits, including the integration of enhanced legal insurance for criminal proceedings, the JuraCheck® legal advice service, and other new legal insurance features. Customers can also choose between different levels of deductibles: one for legal insurance and a different one for home contents, liability, and residential buildings insurance. Work was carried out to extend the ARAG 'Recht&Heim' all-round cover product line in 2016. Since the first half of 2017, the existing premium package has been joined by a brand-new and attractively priced Komfort package that features a wide range of benefits.

ARAG Allgemeine's 'Business Aktiv' product for commercial policyholders, which offers comprehensive insurance for the self-employed and small businesses, was also expanded in 2016 and launched on the market in 2017. In particular, the new features include the CyberSchutz and CyberSchutz Plus add-on modules as well as ARAG Business Assistance, which is described above. The new CyberSchutz module was developed especially for small businesses, providing them with support in respect of risks, problems, and security weaknesses on the internet, in emails, in online banking, or in their online shop.

ARAG Allgemeine has also received a variety of awards and top ratings that bear witness to the comprehensive, tailored protection that the casualty and property insurer offers its customers. For example, the ARAG Alltagshelfer® and ARAG Alltagshelfer Plus® products won the 2016 Customer Innovation Award of the German Institute for Service Quality. Both the Premium and the Komfort variants of ARAG's accident insurance scored an excellent five-star rating in the product reviews conducted by independent analysts Morgen&Morgen.

Furthermore, ARAG Allgemeine continues to underline its role as Europe's largest sports insurer. The product portfolio was enhanced in mid-2016 with a new insurance solution aimed at sports clubs: The package of services provided by ARAG Sports Insurance can be tailored to each club's requirements and the types of sports that they represent. ARAG Sports Insurance covers clubs' equipment and other property. The product also includes a receivables management module for the collection of outstanding debts as well as extended 'away from premises' cover.

ARAG Krankenversicherungs-AG (ARAG Health) also maintained its successful performance in the year under review and, at the same time, cemented its position as a provider of high-quality supplementary health insurance products in the German market. Tight integration within the ARAG Group accelerates the development of cross-segment products. In 2016, for example, special sales channels were developed for taking out and buying insurance under ARAG's 'KTplus' scale of rates for sickness benefit so that it can be quickly and easily taken out in combination with disability insurance – whether from ARAG or another provider. The concept for employer-financed corporate health insurance was also expanded in the reporting year: Since then, the scale of rates for ARAG's highly attrac-

tive corporate health insurance line has included employee-financed scales of rates for supplementary preventive medicine, dental, and inpatient care insurance – featuring high-class healthcare services on attractive terms and with simplified medical examinations or, where opening offers are available, without any medical examination at all. In 2016, ARAG's extensive, needs-based range of high-performance supplementary nursing care insurance products was also updated and has been adapted to meet the new requirements that came into force in January 2017 under Germany's Second Act to Strengthen Long-Term Care. The nursing care insurance products, which were revised at the start of 2017, close the gaps that exist in statutory nursing care insurance.

Numerous awards and ratings in the year under review once again confirmed the significant value proposition offered by ARAG health insurance. In a 2016 study of the best private health insurance providers conducted by DFSI, a German financial services institute, ARAG health insurance made the top three out of a field of 30 companies. DFSI's quality rating was based on an analysis of substance, product quality, and customer service, and ARAG received an overall grade of 'very good' (1.5) and an AA+ rating. ARAG health insurance scored an excellent 5.5 out of a possible six stars from company rating providers [ascore] Das Scoring. And in the brokerage market, an important area for the private health insurance sector, the Company also maintained its track record when it was rated the best provider of supplementary insurance in 2016 in the quarterly AssCompact-Trends broker survey – taking top spot for the 37th quarter in a row.

A large number of other product reviews underline ARAG's excellent reputation in the market – for both full-coverage and supplementary health insurance. In 2016, the Company secured top ratings from [ascore] Das Scoring. The No. 483 outpatient supplementary scale of rates and the V100BL preventive medicine scale of rates (part of corporate health insurance) both received an outstanding assessment and were awarded the maximum six stars. The full-coverage insurance offered in the Premium scale of rates combination 210/220/529 (5.5 stars) and the 'KomfortKlasse' (five stars) was judged to be excellent, and the latter was even designated 'scale of rates of the month' in November. ARAG's supplementary dental scale of rates DentalPro Z100 was also rated as excellent (five stars).

**Employees, employee skills and qualifications** The ARAG Group relies on a skilled, focused, and highly motivated workforce in Germany and in its international markets to ensure that it delivers on its value proposition. At the end of 2016, the ARAG Group had a total of 2,042 (December 31, 2015: 2,019) employees in Germany. A further 2,011 (December 31, 2015: 1,851) people were employed outside Germany. Alongside vocational training, ARAG attaches huge importance to the skills, qualifications, and professional development of its workforce. ARAG intends to remain one of the best insurers in the market. ARAG operates a web-based skills and qualifications platform known as ARAG IQ enabling all employees to keep their knowledge and capabilities up to date. The continuing professional development (CPD) options include classroom-based seminars, training sessions, and e-learning. The content is wide-ranging and includes executive programs, seminars on personal and social skills, project management training, coaching, and foreign languages. All planned and completed CPD has been centrally recorded in ARAG IQ since 2016.

A further key component in ARAG's strategy for retaining suitably qualified employees in the Group is ARAG myCareer, an in-house talent management program introduced in 2011. This program offers an enhanced set of tools to support recruitment and professional development. It helps employees to plan their development and careers, and at the same time ensures that both specialist and interdisciplinary expertise is retained in the Company.

A fundamental factor in the successful performance of the entire ARAG Group is the targeted internationalization of the business. The growing cross-border integration of corporate units also plays a key role in this development. The ARAG INTandem international professional development program, which was launched in February 2015 with a view to systematically expanding this integration and embedding it in the Group, continued in the reporting year. ARAG's sales academy ensures that continuous, high-quality skills development is provided for ARAG partners in the Field Sales force. This unit offers a broad range of needs-based seminars covering the entire spectrum of knowledge related to sales and the performance of ARAG products.

**ARAG Essentials** The revision of the ARAG Essentials in 2014 included the development of a multifaceted communications concept for the corporate guidelines of the ARAG Group. This strategy included the new ARAG Essentials online tool at [www.ARAG.com](http://www.ARAG.com) and meetings throughout the Group to communicate these guidelines. The ARAG Essentials online tool enables users to explore the world of ARAG Essentials in a virtual environment and find out more about the various ARAG locations. The tool is accessible to both the employees and external users on the Group's website at [www.ARAG.com](http://www.ARAG.com), and is available in twelve different languages. As part of the communication activities for ARAG Essentials 2.0, a values mentoring scheme was set up in March 2015. Since then, the approximately 100 executives in the Group's first level of management have been taking it in turns – in alphabetical order – to carry out mentoring with their team for a one-month period. The scheme will continue until December 2017, and details have been published on the groupwide intranet. Since 2012, the ARAG AWARD has been presented in recognition of exemplary implementation of the ARAG Essentials. Prizes are awarded in three categories (Germany, International, and (German) Sales) to team projects proactively initiated by employees that stand out as models of successful implementation of the principles in day-to-day activities. The winning teams receive their awards at the next ARAG Group Management Conference.

**Corporate responsibility** In the ARAG Group, responsible dealings with employees, customers, and partners are based on a long-term, and therefore sustainable, approach. ARAG positions itself as the internationally successful, innovative quality insurer – independent and family-owned. Starting from this fundamental philosophy, the Company takes its corporate social responsibility very seriously. When Heinrich Faßbender established ARAG more than 80 years ago, he had a clear objective in mind: to enable all citizens to enjoy equality of opportunity before the law. This notion still remains an underlying principle in the ARAG Group – and ensures that a high degree of corporate social responsibility is directly enshrined in the ARAG business model.

Today, ARAG brings together the sustainable management of the business at different levels under the general heading of corporate responsibility: the aim is to ensure that customers and consumers derive the greatest possible benefit from the Group's products and services. ARAG also takes responsibility for its employees and supports suitable social projects. The principles of corporate governance set out firmly established voluntary undertakings, providing the framework for socially responsible activities.

**Codes of conduct for sales** With effect from July 1, 2013, all the German companies in the ARAG Group signed up to the revised GDV code of conduct for the sale of insurance products. This code represents a clear industry commitment to more consumer protection, better quality of advice, development of skills and qualifications for agents, and transparent, mandatory rules for dealing with customers. It thereby establishes the foundations for strengthening trust and confidence in the entire area of insurance broking. It is mandatory for ARAG companies to impose a requirement on the agents in the Core Sales and Partner Sales operations to comply with the code. A number of basic steps are already covered by the ARAG 'Red Thread' advisory approach in Core Sales; furthermore, the promise that customers will receive high-quality products and services is in any case an essential component of ARAG's positioning as a high-quality insurer. In ARAG Partner Sales, very close attention is paid to ensuring that, in the collaboration with brokers, the fundamental rules laid down by the broker associations also correspond to the provisions in the GDV code of conduct. The GDV code of conduct provides for a mandatory audit to be carried out by an independent auditor every two years. All five ARAG companies successfully underwent the initial appropriateness test in 2015 and published a description of the compliance management system that serves as the basis for the test and the positive audit report from the independent auditor, PricewaterhouseCoopers, on the GDV website. The appropriateness test examines whether internal corporate rules reflect the regulations in the code. This approach ensures a high degree of commitment and self-monitoring. The ARAG companies will undergo the follow-up test in spring 2017. The ARAG companies are thus adhering to the promise of high quality defined in the GDV code of conduct in their product brokerage.

**ARAGcare** The ARAG Group is widely regarded as a demanding employer that expects high levels of performance from its workforce. In return, the Group invests in a comprehensive range of services for its employees. The key component is ARAGcare, the corporate health management program.

ARAGcare is aimed at supporting the personal health of employees. The tried-and-tested components include health checks, diverse company sports activities, regular preventive medical services, and health courses. One of the main features of these expanded services is a reorganized return-to-work and disability management system, which is now run by an external partner. In the year under review, greater emphasis was also given to the second pillar of ARAGcare: work/life balance. To this end, ARAG underwent a comprehensive third-party audit with the aim of developing and embedding a sustainable HR pol-

icy that takes into account family requirements and stage of life. Targets were drawn up and set during the course of this project, and the 'audit berufundfamilie' certification is accompanied by an obligation for the Company to achieve these targets by 2017. Numerous measures are already being implemented. Examples include action in connection with the Part-Time Management project, the expansion of teleworking and working from home, an employee assistance program, a new range of courses, and many other individual measures. In 2016, ARAG again received a Corporate Health Award certificate of excellence in recognition of these extensive activities by ARAGcare.

**Corporate social responsibility** ARAG is a family enterprise. As a consequence, ARAG attaches a huge amount of importance to the interconnection between corporate and social responsibility. The independence that ARAG enjoys as a family enterprise means that the assumption of responsibility becomes even more significant because it is incumbent on the ARAG Group to use this independence responsibly. Since March 2014, ARAG has therefore been successfully offering its innovative development project known as Conflict Management in Schools.

Supported by the North Rhine-Westphalia Ministry for Education and Schools, this program is offered to all high schools and vocational colleges in the German state of North Rhine-Westphalia. During the three training cycles so far, a total of 233 teachers, specialists in educational social work, and parents from 65 high schools and vocational colleges in different school districts across the state have taken part. The project is currently running at 19 other schools. The project focuses on the introduction of universal quality standards for conflict management structures, preventive measures, and intervention techniques. Teachers, parents, specialists in educational social work, and school pastors are trained as school mediators and go on to train school students as conflict controllers. The project has been certified under the name ARAG Mediators as a 'Commitment to Action' by the Clinton Global Initiative (CGI).

The 2016 ARAG Educational Day, attended by Sylvia Löhrmann, North Rhine-Westphalia's Minister for Education and Schools, was held in June in the ARAG Tower. Participants from schools all over North Rhine-Westphalia took part in ten workshops on intercultural conflict management and mediation.

Another key area of activity is the internet. It is changing and affecting the lives of people around the globe – including to a large degree the lives of children and young people – but is also bringing risks. Suitable prevention is important to avert these risks. ARAG SE has a comprehensive range of prevention experience and believes that important areas of prevention lie in the long-term development of media skills and in the provision of information and education, as well as the raising of awareness, about the consequences of bullying.

The ARAG Digital Risks Survey, an international trend study conducted by ARAG and the Institute for Cyberpsychology and Media Ethics, was presented in Berlin at the end of May 2016. Leading academics in the field of cyberpsychology from the UK, Italy, the Netherlands, Norway, Poland, Spain, and the US investigated the impact of cyberbullying and provided their assessment of this phenomenon and its future development. The find-

ings show that cyberbullying and cyberviolence are evolving from a phenomenon of youth culture into a social problem affecting all age groups. The experts surveyed particularly highlighted the increasing violation of the right of individuals to privacy when online. From 2017, ARAG will therefore focus more intensely on protecting online privacy rights. Corporate social responsibility at ARAG also extends to the provision of support for the German Children and Youth Foundation (DKJS), specifically in the area of digital education. For 20 years, this charity has been operating projects and programs throughout Germany, helping children and young people have the courage to take control of their own lives and play a role in society. This approach is a perfect match for ARAG's definition of corporate responsibility – and also fits in well with its current commitments. Since 2014, ARAG has been supporting the DKJS as a program partner, helping to raise awareness among children and young people about the challenges presented by cyberlife and the risks from cyberbullying.

'ZEIT für die Schule' is a project promoted by Germany's weekly DIE ZEIT newspaper. The project is the largest nationwide school project run by a German newspaper and aims to foster reading skills as well as introduce children from the age of around 14 or 15 to the medium of newspapers. As part of the project, ARAG supported the publication of free worksheets for teachers in the lower and upper stages of secondary education, the delivery of free copies of DIE ZEIT and special publications for schools covering media studies and what to do after the Abitur high-school diploma, and the preparation of newsletters for teachers.

## Employees

	Dec. 31, 2016	Dec. 31, 2015
<i>(permanent)</i>		
Consolidated companies	3,985	3,811
Total Group	4,053	3,870

## Employees

In 2016, there was a further year-on-year rise in the number of employees across the entire Group, in line with planning. Including the companies not encompassed by the consolidation, 4,053 people were employed as of December 31, 2016 (December 31, 2015: 3,870). The consolidated companies had a total of 3,985 permanent employees as of December 31, 2016 (December 31, 2015: 3,811). The headcount increase was predominantly due to hiring in international branches and subsidiaries. As of the balance sheet date, 49.6 percent of the employees in the ARAG Group worked outside Germany (December 31, 2015: 47.8 percent).

### III. Outlook, Opportunity and Risk Reports

#### Outlook

The ARAG Group operates in a total of 17 countries: Germany, 14 other European countries, the US and, since 2016, Canada. Given the strong international focus of the Group, economic trends in Europe and North America in particular have an impact on business performance.

Future global economic growth is currently subject to many significant risks. As well as ongoing geopolitical issues, these risks also include a crisis-like escalation of political uncertainty in Europe, a renewed flaring up of the European sovereign debt crisis, an unexpected downturn in China's economy, and possible turmoil in international financial markets.

Following a temporary period of weakness in the first half of 2016, the US economy is likely to return to a stronger rate of growth. The recovery in Japan and the eurozone is expected to continue. The pace of growth may falter as monetary policy effects and the positive impact of lower oil prices on real incomes disappear. Reflecting the slight rise in oil prices, inflation will go up again. China's economic output is not predicted to slump, and other emerging markets will probably maintain the process of stabilization that they have begun. Overall, the German Council of Economic Experts anticipates that the moderate rate of global economic growth will continue, forecasting a rise in economic output of around 2.8 percent in 2017.

Political developments in Europe demand particular attention. One major concern is that the future political and economic relationships between the United Kingdom and the European Union have not yet been clarified. So far, the vote for Brexit has not had any substantial adverse effects on the real economy. This indicates that the prevailing expectation is that a solution will be found that will limit the damage to the economy. If the two sides cannot resolve their political differences, much greater effects are likely to be felt in the UK in terms of investment, trade, and employment. However, Europe's political risks are not restricted to the uncertainty surrounding Brexit. In many member states, parties on the fringes of the political spectrum are enjoying strong popularity. This brings with it the danger of growing political risk. Moreover, a number of member states have unstable governments. At the end of December, for example, Italy held a referendum on constitutional reforms. The lasting political impact of the vote's outcome is not yet clear to see. The eurozone is also heavily affected by the banking sector's unresolved problems, which have mainly been created by low levels of capitalization and the still high volumes of non-performing loans, e.g. in Italy and Portugal. For the eurozone as a whole, the German Council of Economic Experts predicts that economic output will increase by 1.4 percent in 2017.

Germany's upturn is likely to continue this year. Although the growth in real gross domestic product is expected to drop to 1.3 percent, 0.4 percentage points of this slowdown in the pace of growth is due solely to there being fewer working days in 2017. Excluding this one-off effect, the German economy would expand at virtually the same rate as in

2016. It can be assumed that capacity utilization in manufacturing will continue to rise. The expansionary monetary policy of the European Central Bank (ECB) will probably play a significant part in the German economy's upturn. The effect of the ECB's unconventional measures has been to considerably improve the foreign trade environment for German exports since mid-2014, despite muted global demand. Although currently in a good position, the German economy is not immune to the performance of the rest of the euro area. A marked downturn in the other eurozone countries or an unexpected appreciation of the euro could cause the increase in production to slow down significantly.

One of the factors fueling the sustained upturn is the sharp rise in consumer spending and house-building. This is a reflection of the continued robust health of the labor market, as can be seen from the steady growth of employment. The number of people in employment is predicted to increase by more than 400,000 to a total of 44.0 million in 2017. Nevertheless, a major challenge for German economic policy will be to integrate into the job market those who remain unemployed and a rising number of refugees who have been granted asylum. Disposable income is expected to carry on increasing in the forecast period as conditions in the labor market continue to improve. Pension adjustments made in mid-2016 will also push up monetary welfare benefits in 2017. Consumer spending is therefore predicted to go up by 1.3 percent this year. A higher rate of inflation is also likely in 2017, firstly because energy prices will probably increase and secondly because the core inflation rate is slowly rising due to growing capacity utilization in manufacturing. The average rate of inflation is expected to be 1.6 percent.

The insurance industry will not remain unaffected by the above trends. One of the factors taken into account in the latest forecasts of the German Insurance Association (GDV) is that heightened uncertainty caused, for example, by geopolitical risks is one of the major influences on current macroeconomic conditions. Any change in the projected economic growth could therefore also have an impact on business trends in the insurance industry.

Insurers continue to be faced by challenges caused by an unmistakable trend toward fiercer competition.

As in prior years, other action priorities include the increasing differentiation between customer groups and the need to respond to demographic change. In addition, continuous shifts in insurance markets are being brought about by changes in the product landscape, some of which (such as unisex rates or the pluralization of sales structures) are far-reaching.

One transformation that is clearly becoming increasingly important is the digital revolution. The digitalization of the financial sector is increasing the pressure for change in the rather conservative insurance industry. There is a need to open up additional sales, service, and communication channels – both for companies and for consumers. Other technologies such as telematics are beginning – at least in selected European markets – to have an impact on the realignment of product and pricing policy. 'Either-or' concepts are not sufficient in this context because the market is not populated exclusively by online-

only customers. Whether consumers decide to opt for a digital offering or not depends on the product, the target group, and sentiment. Ultimately, the goal is to offer consumers easy, barrier-free access to insurance benefits. Such an overarching approach is crucial to being able to address the fundamental changes in customer behavior in the digital age. Online business models will therefore soon no longer be aimed at particularly price-sensitive customers but will become an integral component – configured for maximum ease of use – in the range of services provided by each and every insurance company.

The digitalization of legal services is creating new and rapidly increasing challenges, especially for legal insurance providers. One particular example is provided by simpler legal services that are now being offered by dedicated service providers: legal tech companies. It is important to get involved in these trends and take steps to meet new customer requirements, taking account of the special legal requirements in this area, especially in Germany. With the latest technology, it has already been demonstrated that certain legal services can be provided perfectly well via digital platforms. The task is to proactively and systematically seize business opportunities within these parameters.

A whole host of possible digital services for customers are also emerging for health insurance providers. Again, digital channels for communicating with customers need to be significantly improved. Such projects will be implemented in the forecast period.

For property insurers, the main source of risk is the much-discussed climate change that has taken place in past years and decades. Events in early summer 2016 once again showed that natural disasters are an increasingly important issue. In summer 2015, however, politicians had decided against mandatory insurance for natural disasters. Instead, the measures to be taken include national and state-level natural disasters insurance campaigns and the establishment of a country-wide natural disasters portal. The German National Meteorological Service (DWD) and the GDV have launched a new heavy rain project in order to significantly improve the future forecasting of flooding caused by heavy rain so that insurance cover that is more suited to the level of risk can be calculated. The federal government also wants to cut greenhouse gas emissions in Germany to zero by 2050. The insurance industry has contributed its expertise to the development of a strategy, and the sector's experts are also working on new building regulations for Germany and Europe.

As before, sales activities in the German insurance industry are being made more difficult because the market is very mature. Opportunities for further premium growth and for additional expansion of in-force business are largely limited to customers who are switching between insurers. This trend will continue going forward. Consequently, premium growth will most probably be rather modest in the insurance industry. The GDV forecasts growth of up to 1.0 percent for the German market in 2017. Assuming that there is no unforeseen deterioration in the macroeconomic environment, premiums in the casualty and property insurance segment are expected to be up by around 2.1 percent this year. In the case of legal insurance, the GDV predicts a rise in premiums of 4.5 percent in

view of the opportunities to adjust premiums. As in prior years, there is a chance in general accident insurance that the impetus from growth will help to offset the persistent portfolio erosion. The overall result is that premium growth in this insurance segment is likely to be slight at 0.5 percent.

The ARAG Group met the forecasts made last year for the 2016 reporting year. It grew overall, is again generating significant stable earnings, and continues to have a sound level of funding. As expected, the expansion of new business did not cause the claims ratio to rise, and this ratio in fact fell slightly. The cost ratio for the ARAG Group did not increase compared with 2015 either and was actually slightly lower year on year. The forecasts for the individual segments were also met. The legal insurance, casualty and property insurance, and health insurance businesses all provided – in some cases significant – growth impetus, while their contributions to earnings were in line with the budget. In life insurance, the forecast of a substantial drop in the number of new policies underwritten along with declining premiums proved accurate. This effect was compounded by the decision made in 2016 to sell the shares in ARAG Lebensversicherungs-AG, a process which was also initiated in 2016. In terms of earnings, the ARAG Group underlined its operating efficiency as expected by posting another very good underwriting result and significantly increasing its consolidated net income.

Looking ahead, the ARAG Group has laid the foundations for a strong performance in the forecast period. By selling the shares in ARAG Lebensversicherungs-AG, the Group is realigning itself in this phase of low interest rates and embarking on a fundamental process of change. It is therefore forging ahead with its strategy of two-dimensional diversification, which will have an even stronger influence on ARAG in the future. As a result of concentrating on property insurance and health insurance, the Group will initially slim down its balance sheet with a decrease of around €215 million in premium income and a reduction of €2.8 billion in investments. Risk exposures in the policy portfolio and in investments will improve markedly without the life insurance business.

The ARAG Group expects business performance to remain good over the forecast period despite the unstable macroeconomic conditions. With the planned sale of the life insurance business, ARAG is taking a very logical step in response to the protracted phase of low interest rates. Going forward, the Group will focus on property and health insurance and will further internationalize its legal insurance business. The planned changes represent a shift of historic proportions for ARAG. The Group will thereby considerably reduce its vulnerability to attack from the financial markets. In view of the inherently robust profitability of the insurance business, ARAG is prepared to accept the associated loss of possible sources of income. Premium income will also decrease during the forecast period due to the life insurance segment no longer being included. The sale is subject to approval by the German Federal Financial Supervisory Authority (BaFin).

The Group's other segments will maintain their path of growth. In the medium term, the decline in premiums in the life insurance segment will be more than made up for by the other segments. Profit expectations for the forecast period are much lower. In the coming years, ARAG will continue to be associated with stable income – particularly given

its good underwriting profit and a sustained, sound level of funding. The Group will benefit from the modern international structure of its business based on branches and subsidiaries, and from its diversification strategy. Strategically, ARAG will focus on increasing the use of digital technologies in its products and processes, introducing digital services, and making targeted inroads into fast-growing international markets. The share of the Group's sales revenue generated outside Germany will increase as a result of further internationalization.

Preparatory work aimed specifically at meeting new regulatory requirements – necessitating additional reporting and documentation – has already been completed. Approval from BaFin to use a partial internal model to determine capital requirements underlines the profound solidity of the ARAG Group.

A cautious investment strategy has stood the Group in good stead in the years since the European sovereign debt crisis in 2008. Interest rates are expected to rise in the medium term as the European Central Bank comes under increasing pressure to change its policy of zero interest rates and follow the lead of the US Fed in starting to raise rates once again.

The Company regularly updates its strategy, aligning it with the prevailing conditions. This strategy is always codified in the corporate guidelines, the ARAG Essentials. These guidelines help the Management Board to ensure that the focus and positioning of managers and employees are reliable and transparent. The growing corporate social responsibility requirements are also taken into account.

ARAG is continuing to concentrate on providing specific, beneficial services – solutions that customers can try out straight away. In the reporting year, it introduced alternative payment systems for policies taken out online, making ARAG a trailblazer in the market. Customers can now also use these systems to make recurring premium payments. The new ARAG Wallet-Card was recently launched. This service card for smartphones gives customers a very good overview of their insurance policies and insurance cover. The list of the various digital services being steadily introduced – a process that began almost two years ago – is thus growing ever longer. Consumers appreciate ARAG's great agility in this regard. The high number of policies for ARAG products that continue to be concluded online indicates that the needs of the relevant target groups are being addressed appropriately.

Over the forecast period, the Group will keep to its conservative, earnings-oriented operating policy.

The Group's projections for the period vary depending on the segment involved.

In the legal insurance segment, the Group expects to see further growth in gross premium income, although market conditions will be very different across many European countries.

In the German market, the recent significant expansion in the legal insurance business is likely to continue. The strong rise in premiums in 2016 confirms that ARAG SE has returned to a path of growth for the long term in Germany. The combination of product

innovation, high-quality claims processing and services, and a sustainable sales strategy are laying the foundations for further successful growth. ARAG is therefore predicting a continued rise in premiums from the German legal insurance business in 2016.

The international branches and subsidiaries will continue to provide growth stimulus in the forecast period to a degree similar to that in 2016. This takes into account the fact that there will still be challenging market environments. The Group has noticed that business in southern Europe is recovering, aided by its provision of combination products offering cover through legal-insurance-related special service packages. In the US, the Company is carrying out fundamental groundwork in order to improve its business base. It has successfully applied for permission to operate in additional federal states where ARAG is currently not directly represented and instead underwrites policies through a fronting partner. This approval gives the Group the option to be directly represented in those states. ARAG will also remain on a path of growth in its Scandinavian markets and, in particular, intends to step up business in Sweden and Denmark.

The growth in premiums is unlikely to lead to an increase in the claims ratio. It will also be possible to limit the adverse effects in the forecast period from potential cumulative claims in connection with the emissions issue affecting VW vehicles.

The cost ratio for the ARAG Group increased slightly in 2016. This is expected to rise in 2017 and subsequent years because of the planned sale of the life insurance business.

The casualty and property segment brings together ARAG's property, liability, and accident insurance business outside the legal insurance segment. To a lesser extent, legal-insurance-related special service package business in individual international markets is also allocated to the casualty and property segment. In the German market, the Group is once again generating a good level of premium growth in this segment after bringing about a turnaround similar to that in the legal insurance business. This uptrend in the segment will also be sustained. Over the forecast period, the action already initiated to consolidate the portfolio and expand new business will have a further impact. The casualty and property segment remains clearly focused on private customers and is characterized by very efficient claims management. This is one of the reasons why this segment is one of the most profitable units in the ARAG Group. Assuming that no relevant major claims events occur, the segment will be able to achieve a combined ratio of well below 100 percent in the forecast period. The Group predicts that the financial performance of this segment will continue to be very good.

In the forecast period, the health insurance segment will continue to strengthen its position as ARAG's largest business line in the German market. ARAG plays a special role in the market based on its clear strategic focus on high-quality cost-share insurance. It is therefore somewhat more independent from decisions affecting the strategic direction of health policy. The Group is conscious of this special position and will therefore adopt a systematic approach to continue to strengthen this area of business. In the case of supplementary insurance, supplementary nursing care insurance will become increasingly important in the portfolio of products. Corporate health insurance is also becoming another important area of business for ARAG.

Overall, the Group expects to see dynamic growth with a stable level of cancellations/lapses in the cost-share insurance business over the next few years.

Against the backdrop of further premium growth, ARAG Health is paying particular attention to implementing more improvements in the efficiency of application procedures and the processing of benefits. As in other segments, the Group is focusing in the health insurance segment on an expansion of IT infrastructure with a view to further streamlining time-consuming processes in supplementary insurance.

Despite the forecast expansion in business, ARAG anticipates that the claims ratio in this segment will remain steady.

Operating performance is not the only factor that has affected the profitability of health insurers. Their financial performance has also been significantly impacted by trends in financial markets. The long period of low interest rates has not only hit life insurance companies but also had adverse implications for health insurers because of the frequent need to adjust discount rates. The ARAG Group continues to take a conservative approach to capital market activities and has also moderately adjusted its discount rate for health insurance.

The health insurance segment is predicted to secure a growing share of the market in 2017 and 2018.

Even after selling its life insurance business, ARAG will still be able to offer life insurance products to its customers. Given the great importance of being able to provide comprehensive, needs-based advice for customers, offering such products is essential. In fact, the Company's Core Sales organization began selling life insurance from Alte Leipziger at the end of 2016. The partnership is highly successful and has got off to a smooth start.

The ARAG Group managed to raise its profit before tax and before non-controlling interests to €86.8 million in 2016. The very good operating efficiency of the Group was a major contributing factor. Traditionally, ARAG has attached great importance to generating a good level of underwriting earnings on an ongoing basis to enable it to offset some of the capital market volatility. The Group will continue to pursue this business policy consistently over the forecast period. The ARAG Group therefore anticipates an equally good level of earnings over the next few years.

As in previous years, it is currently scarcely possible to arrive at any kind of reliable forecast regarding trends in capital markets. No one can realistically predict how financial markets will be affected by the growing political uncertainty caused by the UK's vote to leave the European Union or the new uncertainties created by the outcome of the US election. The ARAG Group is therefore assuming that conditions in financial markets will remain challenging and that the period of low interest rates will continue. In particular, the Group's investment income will decline significantly once the process to sell the life insurance business has been completed. Given these circumstances, the Group predicts that the net gains on investments in the 2017 forecast period will be weaker.

Taking into account the opportunities and risks currently discernible, the ARAG Group forecasts that business performance in 2017 will remain steady and sound. Overall, the Group will continue to grow and once again demonstrate the strength of its earnings power.

### Opportunity report

Based on the structure of its business, ARAG has one of the highest proportions of international business among German insurers. Almost 35 percent of premium income in the ARAG Group is generated from international business. This structure gives rise to opportunities and risks for the Group.

The excellent international diversification in the ARAG Group makes it more independent of the trends in individual national markets. This applies particularly to the very mature German legal insurance market, which offers few genuine growth prospects. Germany is nevertheless ARAG's traditional core market and thus remains important to the Group. The good level of growth achieved from the legal insurance business in Germany, the original home market, also serves as a significant point of reference for the international business. The strategy of the ARAG Group for the whole of the legal insurance business is to continue the international diversification of this segment.

The international structure of the ARAG Group is the logical business consequence of the advanced saturation of the overall German market and the highly varied economic trends within Europe and around the globe. The legal insurance markets outside Germany still offer significant growth potential. ARAG is focusing considerable effort on exploiting this potential with a view to achieving further growth in the Group. In this regard, ARAG attaches great importance to taking into account the particular features of the market in each country.

Responsibilities are distributed throughout the ARAG Group so that the position enjoyed by the ARAG brand in the German market will be further consolidated and improved by the strengthening of the non-legal-insurance segments. This two-dimensional diversification strategy in the Group is also enabling ARAG to move away from the original tightly focused positioning as a niche provider in Germany. A domestic specialist insurer concentrating solely on one line of business is considerably more susceptible to risk. The strategic approach at ARAG is therefore one of active risk reduction and is based on spreading risk evenly across all markets and segments. The extended period of low interest rates has particularly demonstrated that this is the right approach, which offers both advantages and disadvantages for ARAG. In Germany, the low interest rates are adversely impacting the pension products business. At the same time, the trend in interest rates is supporting the economic recovery in southern Europe, thereby boosting business performance in this region. The Group is also benefiting from its focus on property and health insurance business. The future of the ARAG Group will therefore not be decided by the life insurance segment, but by the capacity of the Group to continue expanding its key domestic and international operations with the level of profitability achieved to date.

To manage the international structure of the ARAG Group, the Management Board is supported by a Group Executive Committee (GEC). This committee comprises the members of the Group Management Board, representatives of the main European branches, and representatives of the other insurance segments in Germany. This committee improves the sharing of information between the European branches and the German insurance companies in the ARAG Group. One of the main objectives of the GEC is to ensure that innovations and market changes are converted more quickly into specific busi-

ness processes, both in Germany and abroad, if the committee believes that these innovations or changes offer clear opportunities for the successful further development of the business.

Overall, the European management structure makes it possible to exploit the diverse opportunities available to the ARAG Group in both its German and international business over the long term. In addition, experience with the new structure has demonstrated that market risks become transparent more quickly for the senior management across all management levels, enabling the Group to respond more promptly.

The ARAG Group will work systematically and energetically to meet the challenges presented by the markets. It will open up opportunities to bring about successful advancement of the business in a demanding and varied market environment. The ARAG Group's clear corporate strategy is to continue the international diversification of the business and significantly expand the share of the international activities in the Group's operations.

## **Risk report**

### **Risk management system**

The assumption of risk is the core business of ARAG as an insurer. This means that its activities aimed at achieving its strategic business objectives naturally involve taking on risks in order to achieve the desired success. To deal with these risks, ARAG has implemented a risk management system of which the operational risk management process forms the core element. Taking a multifaceted approach, including a risk strategy, a limit system, and an own risk and solvency assessment (ORSA), ARAG ensures that its risk management activities to control its business operations remain within the prescribed risk-bearing capacity requirements.

Based on the corporate strategy, the Management Board specifies the risk strategy and defines the capital adequacy requirements and the required limits. Risks are therefore managed in the round, ensuring at all times that the overall risk profile is consistent with the risk strategy. The Supervisory Board deliberates on these matters and receives regular reports on the risk situation.

To implement the risk strategy, the Group has implemented a risk management system, which is the responsibility of the risk management function. This function is performed by the Group Risk Management Central Department. Group Risk Management is separate from the operational departments with profit-and-loss responsibility up to Management Board level and therefore performs the role of an independent risk control function. The Chief Risk Officer of ARAG SE is responsible for the implementation of the risk management system in all Group companies. Group Risk Management bears process responsibility for the risk management system and, by means of quarterly risk reports to the Management Board, ensures that there is comprehensive transparency with regard to the risk position and any changes to the risk position. Group Risk Management is also responsible for refining the risk management system and for drawing up proposals for uniform standards to be applied throughout the Group. The remit of the central department also includes developing models for determining risk-bearing capacity, solvency capital requirements, and the allocation of solvency capital.

Decisions about whether or not to pursue opportunities and/or take on risk are made in the operating units. The roles and responsibilities of all the people involved in the process, such as members of the Management Board, managers, local and central risk controllers and managers, are clearly defined and documented in the ARAG Group's risk management guidelines.

The core element of the risk management system is the risk management process, comprising the identification, analysis, measurement, management, and monitoring of risk as well as risk reporting.

**Risk identification** The aim of risk identification is to identify the emergence of new risks or changes in existing risks at an early stage and to assess them using a standard procedure. For example, risks arising in connection with the development of new markets or the launch of new products are identified, analyzed, assessed, and submitted to the Management Board for decision using an appropriate cross-functional new-product process. Corresponding processes have also been put in place for new investment products and reinsurance instruments. These procedures are also integrated into the existing limit and monitoring processes.

**Risk analysis** To ensure risks are managed appropriately, the influencing factors determining the relevant exposures on the Solvency II balance sheet are examined. These influencing factors are regularly validated to check that they are appropriate for the measurement of risk.

**Risk assessment** All identified risks are constantly quantified using suitable methods and on the basis of systematically captured and continuously updated data. This process also includes checks to ensure that the risk profile is within the specified limits.

The key element in this process is the solvency capital requirement calculated for all quantified downside risk (value-at-risk). The purpose is to ensure that unexpected losses are covered. A partial internal model is used to calculate the solvency capital requirement. The model calculates the maximum loss from risk exposures covered in the model within a specific holding period (one year in this model) and with a specified level of probability (99.5 percent in this model). The loss could arise as a result of unfavorable movements affecting investments or as a result of unexpected developments in the insurance business. The methodology is regularly reviewed using backtesting and validation tests. Stress tests are also continuously carried out in respect of the risk exposures.

**Risk management** The Group's approach is to manage risk where it arises. Operational management of risk is thus carried out by the managers and process owners in those departments where the risks occur. Risk management consists of implementing measures to reduce, mitigate, transfer, and diversify identified and analyzed risks.

**Risk monitoring and reporting** A key element of risk monitoring is examining changes in the risk profile over time, focusing on risk-bearing capacity and utilization of the limits. The risk-bearing capacity of the Group is determined on the basis of the aggregated solvency capital requirement and the eligible own funds that are available. This takes into account the regulatory and internal requirements regarding minimum cover. The actual utilization of limits is determined by reconciling the individual risks assumed and the aggregated risk with the specified limits.

To calculate the limits, the minimum coverage ratio determined by business policy requirements and the eligible own funds are used to determine the maximum permitted solvency capital requirement for the Group. The Management Board sets an overall limit in accordance with its risk tolerance. This overall limit is then apportioned to the risks.

The results from the risk monitoring process and the associated recommendations for action are reported to the Management Board promptly, without restriction, and on a continuous basis.

**Internal control system** The internal control system (ICS) refers to all control and monitoring mechanisms as well as other measures that help to support the effectiveness and profitability of business activities and to identify and minimize risk at an early stage. They also ensure compliance with the applicable laws and regulations, all regulatory requirements, and internal rules.

The ICS is based on the principles, functions, processes, measures, and policies implemented by the Management Board and on statutory and regulatory requirements that ensure the decisions of the Management Board are implemented operationally.

ARAG structures its internal control system in accordance with the 'three lines of defense' model.

The first line of defense is formed by all employees and managers in operational roles. They are directly responsible for the risks and processes in their departments.

The second line of defense is the monitoring of the first line of defense by the interdisciplinary functions Group Controlling, Group Risk Management, and Legal/Compliance and by the Actuarial function. These functions specify standards for the design and monitoring of controls and for the handling of risk.

In the third line of defense, Group Audit conducts internal audits of the functions in the first and second lines of defense within the ARAG Group.

**Internal audit** The Group Audit function, which has been delegated to ARAG SE, is an instrument of ARAG Holding SE's Management Board, to which it is accountable and to which it reports. Group Audit is bound only by the instructions of the Management Board. Following the orders issued by the Management Board, Group Audit examines the opera-

tional and organizational structure as well as the internal control system for all operating and business processes from a risk perspective, including those that have been outsourced to other companies.

The Management Board makes sure that Group Audit carries out its duties autonomously and independently of the units that it audits, particularly in respect of its audit planning, audit procedures, and evaluation of audit results.

So that it can fulfill its role and responsibilities properly, Group Audit does not get involved in operational processes. Employees in Group Audit are not permitted to be assigned tasks that would conflict with Group Audit's independence within the ARAG Group and are not allowed to carry out non-auditing work or operational activities. Group Audit itself does not have any authority to issue instructions to employees in other departments.

### Individual risks

**Underwriting risk in indemnity, liability and accident insurance, and in legal insurance** Underwriting risk is the risk of a loss or adverse change in the value of insurance liabilities arising from inadequate pricing and inadequate provisioning assumptions. These losses result from:

- Premium/reserve risk: fluctuations in the timing, frequency, and severity of insured events and in the duration of claims settlement and the amount involved.
- Catastrophe and accumulation risk: significant uncertainties regarding pricing and assumptions in respect of the recognition of technical provisions for extreme or exceptional events.
- Lapse risk: changes in the level or volatility of the rates of insurance policy lapses and terminations.

These risks are measured with an internal model. Using a simulation, the losses and adverse changes in liabilities that could occur within one year are forecast. The value of the risk equates to the negative simulation result expected only every 200 years (1 in 200 year event). Each risk is measured separately. For premium and reserve risk, specified criteria are used to aggregate historical losses into groups of risks sharing similar characteristics. These are then used for 200,000 simulations of future unexpected claims and/or required additions to reserves. Losses are simulated in the same way for catastrophe and accumulation risk; such losses may arise from natural disasters, large claims caused by people, or cumulative claims in the legal insurance business. Lapse risk is calculated on the basis of exceptional cancellations in the past. The actual underwriting risk arises from the aggregation of the individual risks, taking diversification effects into account.

The consistency of the insurance business and the adequacy of the claims provisions at all times can be seen in the following disclosures on the changes in the claims ratio for the entire direct insurance business over the last ten financial years.

### Changes in claims ratio

Financial year	Claims ratio, gross, total		Settlements
	<i>FY ratio</i>	<i>Financial statements</i>	<i>% of initial reserve</i>
2016	55.9	50.3	4.7
2015	58.0	51.6	6.1
2014	60.2	55.4	3.6
2013	61.3	55.3	5.9
2012	62.6	50.9	7.0
2011	60.3	54.5	4.1
2010	66.7	61.3	4.2
2009	66.4	58.0	6.5
2008	65.2	55.4	7.7
2007	66.8	62.6	3.5

At operational level, underwriting risk arising from indemnity, liability and accident insurance, and from legal insurance is managed by means of underwriting, premium, and reinsurance policy measures.

**Underwriting risk in health insurance** Underwriting risk is the risk of a loss or adverse change in the value of insurance liabilities arising from inadequate pricing and inadequate provisioning assumptions. These losses result from the following three risk components and their associated sub-risks:

1. Risk from health insurance policies that are operated on an actuarial basis comparable to that of indemnity insurance:
  - Premium and reserve risk: fluctuations in the timing, frequency, and severity of insured events and in the timing of claims settlement and the amount involved.
  - Lapse risk (indemnity insurance): changes in the level or volatility of the rates of insurance policy lapses, terminations, renewals, and surrenders.
2. Risk from health insurance policies that are operated on an actuarial basis comparable to that of life insurance:
  - Mortality risk: changes in the level, trend, or volatility of mortality rates, where an increase in the mortality rate leads to an increase in the value of insurance liabilities.
  - Longevity risk: changes in the level, trend, or volatility of mortality rates, where a decrease in the mortality rate leads to an increase in the value of insurance liabilities.
  - Disability-morbidity risk: changes in the level, trend, or volatility of disability, sickness, and morbidity rates.

- Expense risk: changes in the level, trend, or volatility of the expenses incurred in servicing insurance or reinsurance contracts.
  - Revision risk: changes in the level, trend, or volatility of the revision rates applied to annuities due to changes in the legal environment or in the state of health of the person insured.
  - Lapse risk (life insurance): changes in the level or volatility of the rates of insurance policy lapses, terminations, renewals, and surrenders.
3. Risk from health insurance policies under which claims are made as a result of catastrophes:
- Mass accident risk: the risk of having many people in one location at the same time, causing mass accidental deaths, disabilities, and injuries with a high impact on the cost of medical treatment sought.
  - Accident concentration risk: the risk of having concentrated exposures due to densely populated locations, causing concentrations of accidental deaths, disabilities, and injuries in the event of the mass accident scenario described above.
  - Pandemic risk: the risk of having a large number of non-lethal disability and income protection claims and where victims are unlikely to recover as a result of a pandemic.

These risks are measured with the standard formula. Depending on the risk involved, prescribed factors or stress scenarios are used in order to determine their impact on changes in the fair value of the liabilities. One of the methods used by the Group for this purpose is the inflation-neutral measurement method. The sub-risks determined in this way are aggregated into the three risk components for health insurance. The actual underwriting risk arises from the further aggregation of these three components, taking diversification effects into account.

At operational level, underwriting risk arising from health insurance is managed by means of underwriting, benefits, and reinsurance policy measures.

**Underwriting risk in life insurance** Underwriting risk is the risk of a loss or adverse change in the value of insurance liabilities arising from inadequate pricing and inadequate provisioning assumptions. These losses result from:

- Mortality risk: changes in the level, trend, or volatility of mortality rates, where an increase in the mortality rate leads to an increase in the value of insurance liabilities.
- Longevity risk: changes in the level, trend, or volatility of mortality rates, where a decrease in the mortality rate leads to an increase in the value of insurance liabilities.
- Disability-morbidity risk: changes in the level, trend, or volatility of disability, sickness, and morbidity rates.

- Expense risk: changes in the level, trend, or volatility of the expenses incurred in servicing insurance or reinsurance contracts.
- Lapse risk: changes in the level or volatility of the rates of insurance policy lapses, terminations, renewals, and surrenders.
- Catastrophe risk: significant uncertainties regarding pricing and assumptions in respect of the recognition of provisions for extreme or exceptional events.

These risks are measured with the standard formula. The changes in the fair value of liabilities are determined in the stress scenarios on the basis of the actuarial assumptions that have changed. One of the methods used by the Company for this purpose is the industry simulation model. The actual underwriting risk arises from the aggregation of the sub-risks, taking diversification effects into account.

These risks are measured on the basis of the actuarial cash flows determined from a projection of the insurance policies, taking account of best-estimate assumptions about biometrics (e.g. mortality, disability) and customer behavior (e.g. cancellation). These assumptions are largely derived from company-specific, historical data from life insurance policy portfolios. If this base data is insufficient, e.g. in the case of smaller portfolios, assessments from experts and the experience of other market participants are used. The calculation parameters for biometrics and cancellations used in the calculation of the technical provisions are thus considered appropriate.

At operational level, underwriting risk arising from life insurance is managed by means of underwriting, benefits, and reinsurance policy measures.

**Counterparty default risk** While counterparty default risk attaching to investments is calculated as part of market risk, counterparty default risk in the insurance business is treated separately. Counterparty default risk is the downside risk arising from the unexpected default or deterioration in the credit standing of counterparties and debtors during the next twelve months.

Counterparty default risk is measured with the standard formula. The risk is an aggregation of the solvency capital requirement for receivables from reinsurers and the solvency capital requirement for receivables from policyholders/insurance brokers. This aggregation takes account of specified correlations.

The risk of default on receivables from reinsurers is modeled on the basis of the information available and proportionality considerations. The reinsurers' individual credit ratings are explicitly used. The breakdown by rating class of the total amount of receivables from reinsurers is as follows: AA- 1.9 percent, A+ 9.7 percent, BBB+ 7.8 percent, BBB- 51.6 percent, and no rating 29.0 percent.

Default risk in connection with reinsurance contracts is managed in accordance with the reinsurance strategy, which is reviewed at regular intervals.

To measure the risk of default on receivables from policyholders and insurance brokers, a constant factor is applied to the fair value of the relevant exposures on the Solvency II balance sheet. As of the balance sheet date, receivables from policyholders more than 90 days past due amounted to €28.1 million (December 31, 2015: €17.3 million). The average default rate over the last three years as of December 31, 2016 was 12.1 percent. Receivables from policyholders are managed by means of an automated reminder and dunning process.

**Market risk** Market risk is the risk of loss or of adverse changes to market prices of assets, liabilities, and financial instruments. The risk arises directly or indirectly from the following sub-risks:

- **Interest-rate risk:** changes in the term structure or volatility of interest rates. An assumed increase or decrease of 1 percent in the general level of interest rates would decrease or increase the fair value of the ARAG Group's fixed-income securities by €429.0 million. The breakdown of fixed-income securities is as follows (fair values): of the fixed-income securities – including securities held indirectly through institutional funds – approximately 35.1 percent are accounted for by financial services entities, 32.1 percent by public-sector bonds, and 32.8 percent by bonds of non-financial services entities.
- **Equity risk:** changes in the level or volatility of the market prices of equities. A hypothetical fall in equities markets of 20 percent would cause a loss in fair value of €103.5 million.
- **Property risk:** changes in the level or volatility of the market prices of real estate.
- **Spread risk:** changes in the level or volatility of credit spreads over the risk-free interest-rate term structure. The breakdown of interest-bearing investments by rating is as follows:

#### Fixed-income securities by rating class

(Proportion (%) by fair value)

AAA	18.2
AA	23.1
A	23.5
BBB	29.7
BB	4.0
B	1.3
CCC	0.0
CC	0.0
C	0.0
D	0.0
Not rated	0.2

- Currency risk: changes in the level or volatility of exchange rates.
- Concentration risk: all risk exposures with a loss potential that is large enough to threaten solvency or financial position.

These risks are measured with the standard formula. New fair values of investments and liabilities are determined in the stress scenarios for interest rates, share prices, real estate prices, credit spreads, credit ratings/defaults, and exchange rates. The actual market risk arises from the aggregation of the sub-risks and from concentration risk, taking diversification effects into account.

The strategic asset allocation is defined in order to manage the risks. This allocation is used to optimize the investment portfolio so that the desired risk/return ratio can be achieved. Portfolio management is based on the prudent person principle and follows the related regulatory requirements. Interest-rate risk is contained separately by means of asset-liability management. In addition, derivatives are used to hedge changes in interest rates, share prices, and exchange rates. Investments in hedge funds, the funding of investments by borrowing, and the sale of shares not owned by the ARAG Group (short selling) are not permitted.

To be able to achieve the guaranteed minimum return in life insurance business, the ARAG Group pursues a policy of differentiation in investment portfolios in terms of maturity and borrower structure. The current portfolio of fixed-income investments is generating a return that is higher than the current guaranteed return for customers. New investments are made exclusively in securities with a specified minimum rating and with maturities that match the interest-rate trend projected by the Group. The ARAG Group is also under a statutory obligation to recognize provisions and hold other resources in reserves to ensure that it is able to satisfy the guarantees. In an environment of long-term low interest rates, these resources are added to the actuarial reserve in the form of the supplementary change-in-discount-rate reserve.

**Liquidity risk** Liquidity risk is the risk that insurance companies are unable to realize investments and other assets in order to settle their financial obligations when they fall due.

Currently, there is no regulatory solvency requirement for the coverage of liquidity risk so it is not measured. Instead, the monthly excess liquidity cover and liquidity shortfall are calculated on a rolling basis.

Each line item on the balance sheet is assigned to a liquidity class so that the liquidity of the non-trading portfolio can be adjusted if necessary. To ensure the Company can always meet its due liabilities, most investments are made in the 'available-for-sale at short notice' liquidity class.

The liquidity planning is updated constantly so that liquidity can be managed. The Group thus has early warning of whether it will require liquidity in the coming months.

**Operational risk** Operational risk is the risk arising from inadequate or failed internal processes or systems, employee misconduct, or unexpected external events that disrupt or even prevent business operations. Operational risk also encompasses legal risk but does not include reputational risk or risks arising from strategic decisions.

The Group uses the standard formula to determine the solvency capital requirement.

Measurement for operational purposes is derived from the estimated gross and net values of each individual operational risk based on the risk's probability of occurrence and its impact on the income statement. The probability of occurrence describes the likelihood that an operational risk will materialize within a defined period. The scale is calibrated for a period of one year. Both a qualitative and a quantitative estimate of the impact can be prepared. In the case of a quantitative estimate, the risk is classified directly using a risk matrix. With a qualitative estimate, the impact is determined by comparing the risk matrix classification with the class limits. This risk matrix enables the risks to be prioritized. As risks are measured using subjective estimates carried out by experts, the employees responsible have an additional instrument, the loss event database, that helps them to determine the values. This contains data on all loss events that have occurred in the past and their actual impact on the income statement.

Specific measures are agreed upon and carried out in order to manage the identified risks at operational level.

### Overall risk position

**Risks to the Group's survival as a going concern** There are no internal or external risks that could have a permanent adverse impact on the net assets, financial position, or results of operations of the Group. One external risk that has been increasing for some time now is the period of ultra-low interest rates, which is putting a huge amount of pressure on the Group's life insurance business and on the German life insurance industry. The overall risk position does not currently point to any trends in 2017 that could jeopardize the continued existence of the Group as a going concern or cause a significant negative impact on net assets, financial position, or results of operations.

**Risk position** New regulatory requirements for the quantification of the risk position have been in force since January 1, 2016. The regulatory minimum capital requirement pursuant to section 122 VAG is met in full. Moreover, the eligible own funds are significantly higher than the solvency capital requirement calculated in accordance with section 97 VAG. Further details of the coverage situation can be found in the solvency and financial condition report.

# Consolidated Financial Statements

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## Consolidated Balance Sheet as of December 31, 2016

### Assets

(€)

#### A. Intangible assets

1. Goodwill
2. Miscellaneous intangible assets

#### B. Investments

- I. Land, land rights and buildings, including buildings on third-party land
- II. Investments in affiliated companies and equity investments
  1. Shares in affiliated companies
  2. Lending to affiliated companies
  3. Investments in associates
  4. Miscellaneous equity investments
  5. Lending to long-term investees and investors
- III. Miscellaneous investments
  1. Equities, investment fund shares/units, and other variable-yield securities
  2. Bearer bonds and other fixed-income securities
  3. Loans secured by mortgages or land charges and fixed-income receivables
  4. Miscellaneous lending
    - a) Registered bonds
    - b) Promissory notes and loans
    - c) Loans and prepayments for certificates of insurance
    - d) Sundry lending
  5. Bank deposits
  6. Other investments

#### IV. Deposits with ceding insurers

#### C. Investments for the account and at the risk of life insurance policyholders

#### D. Receivables

- I. Receivables from direct insurance business from
  1. policyholders
    - a) Claims due
    - b) Claims not yet due
  2. insurance brokers  
of which from affiliated companies: € 0.00 (Dec. 31, 2015: € 428.26)
- II. Receivables from reinsurance business
- III. Miscellaneous receivables  
of which from affiliated companies: € 757,283.36 (Dec. 31, 2015: € 754,725.34)  
of which from other long-term investees and investors: € 3,033,335.03 (Dec. 31, 2015: € 3,000,000.00)

#### E. Miscellaneous assets

- I. Land held for sale and other inventories of non-insurance companies
- II. Property and equipment and inventories
- III. Current bank balances, checks and cash on hand
- IV. Other assets

#### F. Prepaid expenses and accrued income

- I. Accrued interest and rent
- II. Miscellaneous prepaid expenses and accrued income

#### G. Deferred tax assets

#### H. Excess of plan assets over pension liabilities

#### Total assets

Note		Dec. 31, 2016	Dec. 31, 2015
	2 p. 74	16,446,994.14	19,805,497.86
	3 p. 74	11,675,365.00	12,490,291.88
		<b>28,122,359.14</b>	<b>32,295,789.74</b>
	34 p. 86		
	4 p. 74	237,092,966.86	243,222,371.53
	5 p. 75		
		1,449,140.76	3,640,697.83
		0.00	221,300.00
		13,515,114.94	12,660,469.69
		5,517,422.64	19,215,285.70
		32,735.82	0.00
		20,514,414.16	35,737,753.22
	6 p. 75	2,432,231,368.42	2,330,465,208.17
	7 p. 75	1,642,813,616.03	1,428,049,048.92
	10 p. 76	88,799,939.30	114,117,759.65
	9 p. 76	1,031,556,459.40	1,050,056,459.40
		697,791,202.11	651,099,912.47
		43,927,845.32	49,050,457.88
	8 p. 76	6,798,348.41	4,378,528.43
		1,780,073,855.24	1,754,585,358.18
	12 p. 76	195,562,200.64	155,089,310.96
		42,118,890.86	25,838,999.10
		6,181,599,870.49	5,808,145,684.98
		44,388,849.23	36,148,718.55
		<b>6,483,596,100.74</b>	<b>6,123,254,528.28</b>
	11 p. 76		<b>298,941,578.67</b>
	13 p. 76		
		55,966,269.75	51,311,531.56
		25,353,139.51	38,267,159.85
		81,319,409.26	89,578,691.41
		27,066,953.08	27,693,072.14
		108,386,362.34	117,271,763.55
		45,605,086.66	44,926,228.09
		30,736,786.68	53,305,046.86
		<b>184,728,235.68</b>	<b>215,503,038.50</b>
		0.00	50,944,304.02
	14 p. 76 15 p. 76	25,201,470.71	25,546,960.74
		150,350,131.84	155,312,016.22
	16 p. 76	46,330,389.71	64,276,256.51
		<b>221,881,992.26</b>	<b>296,079,537.49</b>
	17 p. 76		
		58,361,383.99	58,495,208.75
		10,493,526.31	11,063,131.71
		<b>68,854,910.30</b>	<b>69,558,340.46</b>
	18 p. 76 35 p. 89	<b>23,586,916.89</b>	<b>46,730,199.97</b>
	19 p. 77	<b>3,763.28</b>	<b>6,910.36</b>
		<b>7,298,181,190.32</b>	<b>7,082,369,923.47</b>

## Consolidated Balance Sheet as of December 31, 2016

### Equity and liabilities

(€)

#### A. Equity

I.	Subscribed capital
II.	Revenue reserves
1.	Statutory reserves
2.	Other revenue reserves
3.	Exchange rate reserves
4.	Difference pursuant to section 309 (1) HGB
III.	Net income attributable to the Group
1.	Consolidated net income
IV.	Non-controlling interests
1.	in the capital
2.	in the net income

#### B. Goodwill arising on consolidation

#### C. Subordinated liabilities

#### D. Technical provisions

I.	Unearned premiums
1.	Gross amount
2.	less: portion for outward reinsurance business
II.	Actuarial reserve
1.	Gross amount
2.	less: portion for outward reinsurance business
III.	Provision for outstanding claims
1.	Gross amount
2.	less: portion for outward reinsurance business
IV.	Provision for performance-based and non-performance-based bonuses and rebates
V.	Equalization provision and similar provisions
VI.	Miscellaneous technical provisions
1.	Gross amount
2.	less: portion for outward reinsurance business

#### E. Technical provisions in the life insurance business where the investment risk is borne by the policyholders

I.	Actuarial reserve
II.	Sundry technical provisions

Carried forward:

		Note		Dec. 31, 2016	Dec. 31, 2015
		32 p. 83 40 p. 96			
			200,000,000.00		200,000,000.00
			10,339,995.00		9,663,312.00
			223,959,634.47		205,375,050.02
			12,468,449.13		11,202,980.20
		1 p. 73	- 35,999,890.82		- 35,999,890.82
			210,768,187.78		190,241,451.40
			42,804,068.63		29,261,267.45
			7,827,933.08		7,028,075.48
			313,900.77		- 33,943.57
			8,141,833.85		6,994,131.91
				<b>461,714,090.26</b>	<b>426,496,850.76</b>
				<b>0.00</b>	<b>0.00</b>
		20 p. 77		<b>30,000,000.00</b>	<b>30,000,000.00</b>
		21 p. 77			
			258,223,476.56		253,211,942.05
			- 2,766,334.14		- 2,569,868.75
			255,457,142.42		250,642,073.30
		22 p. 77			
			3,954,990,308.88		3,760,867,925.81
			- 34,081,811.00		- 38,287,710.00
			3,920,908,497.88		3,722,580,215.81
		23 p. 79			
			1,399,696,151.58		1,390,996,663.99
			- 31,207,617.42		- 34,623,109.85
			1,368,488,534.16		1,356,373,554.14
			323,424,352.47		309,232,773.66
		24 p. 80			
			78,610,550.00		65,818,834.00
		25 p. 80			
			18,059,344.80		17,298,705.78
			0.00		0.00
			18,059,344.80		17,298,705.78
				<b>5,964,948,421.73</b>	<b>5,721,946,156.69</b>
			245,822,385.34		250,981,633.25
			41,584,526.69		47,959,945.42
				<b>287,406,912.03</b>	<b>298,941,578.67</b>
				<b>6,744,069,424.02</b>	<b>6,477,384,586.12</b>

## Consolidated Balance Sheet as of December 31, 2016

### Equity and liabilities

(€)

Brought forward:

#### F. Other provisions

- I. Provisions for pensions and other post-employment benefits
- II. Provisions for taxes
- III. Miscellaneous provisions

#### G. Deposits received from reinsurers

#### H. Other liabilities

- I. Liabilities from direct insurance business to
  - 1. policyholders
  - 2. insurance brokers
    - of which to affiliated companies: € 13.87 (Dec. 31, 2015: € 13.21)
- II. Liabilities from reinsurance business
- III. Liabilities to banks
- IV. Miscellaneous liabilities
  - of which tax liabilities: € 20,665,471.25 (Dec. 31, 2015: € 18,316,929.60)
  - of which social security liabilities: € 1,998,559.48 (Dec. 31, 2015: € 2,138,605.22)
  - of which to affiliated companies: € 237,277.65 (Dec. 31, 2015: € 832,124.84)
  - of which to other long-term investees and investors: € 0.00 (Dec. 31, 2015: € 0.00)
  - of which secured by a property lien: € 0.00 (Dec. 31, 2015: € 0.00)

#### I. Deferred income and accrued expenses

#### J. Deferred tax liabilities

#### Total equity and liabilities

		Note		Dec. 31, 2016	Dec. 31, 2015
				<b>6,744,069,424.02</b>	<b>6,477,384,586.12</b>
		26 p. 81		230,811,037.36	239,093,108.26
				16,776,935.12	16,613,486.79
		27 p. 82		95,514,918.73	84,611,054.45
				<b>343,102,891.21</b>	<b>340,317,649.50</b>
		28 p. 82		<b>36,991,408.31</b>	<b>41,226,083.96</b>
		29 p. 82			
			63,801,327.73		45,952,840.76
			30,693,360.65		31,091,077.98
			94,494,688.38		77,043,918.74
		29 p. 82	3,534,870.24		4,059,338.77
		30 p. 83	0.00		32,280,674.42
			59,204,800.55		80,756,196.72
				<b>157,234,359.17</b>	<b>194,140,128.65</b>
		31 p. 83		<b>16,783,107.61</b>	<b>29,301,475.24</b>
				<b>0.00</b>	<b>0.00</b>
				<b>7,298,181,190.32</b>	<b>7,082,369,923.47</b>

## Consolidated Income Statement for the Period from January 1 to December 31, 2016

### Line item

(€)

#### I. Underwriting account for casualty and property insurance

1. Premiums earned for own account

a) Gross premiums written

b) Reinsurance premiums ceded

c) Change in gross unearned premiums

d) Change in reinsurers' share of gross unearned premiums

2. Technical interest income for own account

3. Miscellaneous underwriting income for own account

4. Claims incurred net of reinsurance

a) Payments for claims

aa) Gross amount

bb) Reinsurers' share

b) Change in provision for outstanding claims

aa) Gross amount

bb) Reinsurers' share

5. Change in miscellaneous net technical provisions

a) Net actuarial reserve

b) Miscellaneous technical provisions

6. Expenses for performance-based and non-performance-based bonuses and rebates for own account

7. Own account insurance business operating expenses

a) Gross insurance business operating expenses

b) less: commissions received and profit sharing received from outward reinsurance business

8. Miscellaneous underwriting expenses for own account

#### 9. Subtotal

10. Change in the equalization provision and similar provisions

**11. Underwriting result for own account in casualty and property insurance**

	Note			2016	2015
	33 p. 85	1,159,131,503.00			1,088,344,909.66
		-13,000,424.59			-11,332,762.19
			1,146,131,078.41		1,077,012,147.47
		-4,410,610.54			-8,902,743.78
		220,599.00			467,317.56
			-4,190,011.54		-8,435,426.22
				<b>1,141,941,066.87</b>	<b>1,068,576,721.25</b>
				<b>633,896.00</b>	<b>926,945.02</b>
				<b>1,901,346.15</b>	<b>2,008,907.93</b>
		564,473,901.98			550,880,250.09
		-3,135,571.97			-5,580,978.97
			561,338,330.01		545,299,271.12
		14,966,069.38			6,033,087.42
		2,652,019.30			499,955.03
			17,618,088.68		6,533,042.45
				<b>578,956,418.69</b>	<b>551,832,313.57</b>
			0.00		0.00
			173,548.84		-479,950.43
				<b>173,548.84</b>	<b>-479,950.43</b>
	39 p. 93			<b>0.00</b>	<b>0.00</b>
			488,284,632.90		464,823,347.65
			-3,056,824.62		-1,909,167.91
				<b>485,227,808.28</b>	<b>462,914,179.74</b>
				<b>1,697,562.09</b>	<b>1,720,455.64</b>
				<b>78,768,068.80</b>	<b>54,565,674.82</b>
				<b>-12,791,716.00</b>	<b>-5,782,570.00</b>
				<b>65,976,352.80</b>	<b>48,783,104.82</b>

## Consolidated Income Statement for the Period from January 1 to December 31, 2016

### Line item

(€)

#### II. Underwriting account for life and health insurance

1. Premiums earned for own account
a) Gross premiums written
b) Reinsurance premiums ceded
c) Change in gross unearned premiums
d) Change in reinsurers' share of gross unearned premiums
2. Premiums from the gross provision for bonuses and rebates
3. Income from investments
a) Income from equity investments
b) Income from associates
c) Income from other investments
of which from affiliated companies: € 19,447.12 (2015: € 19,256.21)
aa) Income from land, land rights and buildings,
including buildings on third-party land
bb) Income from other investments
d) Income from reversals of write-downs
e) Gains on the disposal of investments
4. Unrealized gains on investments
5. Miscellaneous underwriting income for own account
6. Claims incurred net of reinsurance
a) Payments for claims
aa) Gross amount
bb) Reinsurers' share
b) Change in provision for outstanding claims
aa) Gross amount
bb) Reinsurers' share
7. Change in miscellaneous net technical provisions
a) Net actuarial reserve
aa) Gross amount
bb) Reinsurers' share
b) Miscellaneous technical provisions
8. Expenses for performance-based and non-performance-based bonuses and rebates for own account
9. Own account insurance business operating expenses
a) Front-end fees
b) Administrative expenses
c) less: commissions received and profit sharing received from outward reinsurance business
10. Expenses for investments
a) Expenses for the management of investments, interest expense and similar charges and other expenses for investments
b) Depreciation, amortization and write-downs of investments
of which write-downs: € 33,999,855.00 (2015: € 3,474,022.49)
c) Losses on the disposal of investments
11. Unrealized losses on investments
12. Miscellaneous underwriting expenses for own account
<b>13. Underwriting result for own account in life and health insurance</b>

Note				2016	2015
	33 p. 85	570,566,972.51			567,713,074.67
		-5,880,855.23			-4,809,811.07
			564,686,117.28		562,903,263.60
		-156,427.84			-203,222.38
		-24,133.61			-41,509.98
			-180,561.45		-244,732.36
				<b>564,505,555.83</b>	<b>562,658,531.24</b>
				<b>37,394,969.64</b>	<b>27,650,295.27</b>
			158,085.46		1,496,677.18
			0.00		0.00
		12,973,433.78			9,635,080.76
		138,788,067.45			150,655,337.46
			151,761,501.23		160,290,418.22
			21,841,961.45		4,552,158.93
			35,448,974.64		39,437,453.92
				<b>209,210,522.78</b>	<b>205,776,708.25</b>
	36 p. 90			<b>1,605,083.54</b>	<b>9,373,246.65</b>
				<b>7,552,659.26</b>	<b>7,395,597.62</b>
		451,983,739.04			432,094,008.87
		-8,074,796.32			-7,913,983.55
			443,908,942.72		424,180,025.32
		8,749,495.45			472,751.52
		-763,473.13			928,248.65
			7,986,022.32		1,401,000.17
				<b>435,922,920.40</b>	<b>422,779,025.15</b>
		-188,963,511.16			-168,835,455.53
		-4,205,899.00			-1,472,053.00
			-193,169,410.16		-170,307,508.53
			6,410,129.73		-2,030,962.07
				<b>-186,759,280.43</b>	<b>-172,338,470.60</b>
	39 p. 93			<b>71,482,360.87</b>	<b>57,635,326.02</b>
		47,010,594.55			50,520,084.87
		15,788,166.52			17,182,841.26
			62,798,761.07		67,702,926.13
			-1,552,489.36		128,670.55
				<b>61,246,271.71</b>	<b>67,831,596.68</b>
			10,866,335.46		6,990,515.03
			12,507,786.94		36,270,872.79
			9,167,415.63		4,516,802.76
				<b>32,541,538.03</b>	<b>47,778,190.58</b>
				<b>7,277,635.77</b>	<b>1,337,576.91</b>
				<b>24,280,125.57</b>	<b>25,827,319.75</b>
				<b>758,658.27</b>	<b>17,326,873.34</b>

## Consolidated Income Statement for the Period from January 1 to December 31, 2016

### Line item

(€)

#### III. Non-underwriting account

1. Underwriting result for own account
a) in casualty and property insurance
b) in life and health insurance
2. Income from investments, unless listed under II. 3.
a) Income from equity investments of which from affiliated companies: € 421,888.65 (2015: € 722,123.23)
b) Income from associates
c) Income from other investments of which from affiliated companies: € 65,695.56 (2015: € 67,222.18)
aa) Income from land, land rights and buildings, including buildings on third-party land
bb) Income from other investments
d) Income from reversals of write-downs
e) Gains on the disposal of investments
3. Expenses for investments, unless listed under II. 10.
a) Expenses for the management of investments, interest expense and similar charges and other expenses for investments
b) Depreciation, amortization and write-downs of investments of which write-downs: € 15,330,177.30 (2015: € 8,155,840.84)
c) Losses on the disposal of investments
d) Transfer of losses from associates accounted for using the equity method
4. Technical interest income
5. Revenue of non-insurance companies
6. Cost of goods and services provided by non-insurance companies to generate revenue
7. Other income
8. Other expenses of which write-downs on goodwill arising on consolidation: € 3,132,819.56 (2015: € 3,132,819.56)
<b>9. Non-underwriting result</b>
<b>10. Profit/loss from ordinary activities</b>
11. Extraordinary income
12. Extraordinary expenses
<b>13. Profit before tax</b>
14. Income taxes of which resulting from the change in recognized deferred taxes: € 23,041,647.08 (2015: tax income of € 5,534,051.07)
15. Miscellaneous taxes
<b>16. Net income for the year</b>
<b>17. of which non-controlling interests</b>

Note				2016	2015
			65,976,352.80		48,783,104.82
			758,658.27		17,326,873.34
				<b>66,735,011.07</b>	<b>66,109,978.16</b>
		563,701.13			875,335.56
		3,907,835.95			3,505,573.04
		14,597,831.16			14,812,892.03
		46,367,178.07			56,609,213.32
		60,965,009.23			71,422,105.35
		9,275,203.49			4,687,940.54
		10,152,336.11			6,144,035.33
			84,864,085.91		86,634,989.82
		11,035,063.08			11,953,505.72
		8,865,331.35			18,797,111.07
		976,812.39			1,914,066.87
		0.00			0.00
			20,877,206.82		32,664,683.66
				<b>63,986,879.09</b>	<b>53,970,306.16</b>
				<b>-633,896.00</b>	<b>-926,945.02</b>
				<b>54,829,662.22</b>	<b>66,640,144.33</b>
				<b>49,546,577.00</b>	<b>62,038,407.15</b>
			29,254,101.17		24,479,721.71
			77,586,028.16		81,500,528.82
				<b>-48,331,926.99</b>	<b>-57,020,807.11</b>
				<b>20,304,141.32</b>	<b>624,291.21</b>
				<b>87,039,152.39</b>	<b>66,734,269.37</b>
	<a href="#">37</a> p. 90		0.00		0.00
	<a href="#">37</a> p. 90		266,844.00		266,844.00
				<b>-266,844.00</b>	<b>-266,844.00</b>
				<b>86,772,308.39</b>	<b>66,467,425.37</b>
	<a href="#">38</a> p. 90		42,225,520.13		35,683,817.83
			1,428,818.86		1,556,283.66
				<b>43,654,338.99</b>	<b>37,240,101.49</b>
				<b>43,117,969.40</b>	<b>29,227,323.88</b>
				<b>313,900.77</b>	<b>-33,943.57</b>

## Notes to the Consolidated Financial Statements

### I. Disclosures on the Basis of Consolidation, Accounting Policies, and Consolidation Methods

#### Legal basis of preparation

ARAG Holding SE is entered in the commercial register of the Düsseldorf local court under the number HRB 66673. Its registered office is ARAG Platz 1, 40472 Düsseldorf, Germany. The consolidated financial statements of ARAG Holding SE and the group management report are prepared in accordance with the requirements of the German Commercial Code (HGB) for large corporations and with the supplementary provisions for insurance companies dated November 8, 1994 (Regulation on the Accounting of Insurance Undertakings, RechVersV), in particular in compliance with the requirements on consolidated accounting pursuant to sections 341i and 341j HGB and sections 58–60 RechVersV and with the German accounting standards (GAS). The latter are applied to the extent that they do not limit accounting consistency and to the extent that they are material to the reporting of the Group's net assets, financial position, and results of operations. The transitional provisions relating to the German Accounting Law Modernization Act (BilMoG) dated May 25, 2009 in section 67 of the Introductory Act to the German Commercial Code (EGHGB) are applied in respect of some of the Group companies. In accordance with section 291 (1) HGB, these consolidated financial statements exempt those group companies that are obliged to prepare consolidated financial statements under section 290 HGB from that obligation.

The consolidated financial statements are presented on the basis of financial statement forms 1 and 4 pursuant to section 58 (1) RechVersV. The forms are supplemented to reflect Group-specific characteristics and items relating to non-insurance business.

The single-entity financial statements of the entities included in the consolidated financial statements are nearly all prepared in accordance with the same accounting policies used by the ARAG Group. With the exception of associates, the financial statements of Group companies that are not prepared in accordance with the requirements of the HGB and RechVersV are reconciled with regard to recognition, presentation, and valuation and brought into line with German accounting standards.

The associates' accounting policies generally differ from German accounting principles. One equity investment based in Switzerland prepares its financial statements in accordance with the Swiss Code of Obligations (OR). The financial statements are not reconciled because the foreign accounting policies are largely similar to those of the HGB.

#### Basis of consolidation

As of December 31, 2016, 36 subsidiaries were included in the consolidated financial statements pursuant to section 301 (1) HGB (December 31, 2015: 38). Two companies were deconsolidated with effect from September 30, 2016 because they were sold to third parties. One Group company was consolidated as an associate pursuant to section 311 HGB.

In 2016, the basis of consolidation excluding associates comprised seven insurance companies (2015: seven), two service companies in the field of information technology and business organization (2015: two), two real-estate management companies

(2015: two), four capital investment vehicles (2015: four), 18 other service companies (2015: 19), and four holding and asset management companies (including the parent company; 2015: five).

**The following companies are included in the consolidated financial statements:**

Name of company	Shareholding (%)
1 Advisory Communications System Inc., Des Moines, Iowa/USA (until November 2, 2016)	100.00
2 AFI Verwaltungs-Gesellschaft mbH, Düsseldorf	100.00
3 ALIN 1 Verwaltungs-GmbH, Düsseldorf	100.00
4 ALIN 2 Verwaltungs-GmbH, Düsseldorf	100.00
5 ALIN 3 Verwaltungs-GmbH, Düsseldorf	92.00
6 ALIN 4 Verwaltungs-GmbH, Düsseldorf	94.01
7 ALIN 1 GmbH & Co. KG, Düsseldorf	100.00
8 ALIN 2 GmbH & Co. KG, Düsseldorf	100.00
9 ALIN 3 GmbH & Co. KG, Düsseldorf	92.00
10 ALIN 4 GmbH & Co. KG, Düsseldorf	94.01
11 ALV Vermögens- und Beteiligungs-Verwaltungs AG, Munich (until September 30, 2016)	92.00
12 ARAG 2000 Beteiligungs-Gesellschaft mbH & Co. KG, Munich	92.00
13 ARAG 2000 Grundstücksgesellschaft bR, Düsseldorf	93.38
14 ARAG Allgemeine Versicherungs-AG, Düsseldorf	100.00
15 ARAG Association LLC, Des Moines, Iowa/USA	100.00
16 ARAG Holding SE, Düsseldorf, <b>Group parent company</b>	100.00
17 ARAG Insurance Company Inc., Des Moines, Iowa/USA	100.00
18 ARAG International Holding GmbH, Düsseldorf (formerly TERRA Gesellschaft für Finanzdienstleistungen und Beratung mbH)	100.00
19 ARAG IT GmbH, Düsseldorf	100.00
20 ARAG Krankenversicherungs-AG, Munich	94.01
21 ARAG Lebensversicherungs-AG, Munich	92.00
22 ARAG Legal Services B.V., Leusden/Netherlands	100.00
23 ARAG Liegenschaftsverwaltungs- und Beratungs-Gesellschaft mbH, Düsseldorf	100.00
24 ARAG Liegenschaftsverwaltungs- und Beratungs-GmbH & Co. Immobilien KG, Düsseldorf	100.00
25 ARAG LLC, Des Moines, Iowa/USA	100.00
26 ARAG North America Inc., Des Moines, Iowa/USA	100.00
27 ARAG Plc., Bristol/United Kingdom	100.00
28 ARAG SE, Düsseldorf	100.00
29 ARAG Service Center GmbH, Düsseldorf	100.00
30 ARAG Services Corporation, Toronto/Canada	100.00
31 ARAG Services LLC, Des Moines, Iowa/USA	100.00
32 CUR Versicherungsmakler GmbH, Düsseldorf	100.00
33 Cura Versicherungsvermittlung GmbH, Düsseldorf	100.00
34 HELP Forsikring AS, Oslo/Norway	100.00
35 Interlloyd Versicherungs-AG, Düsseldorf	100.00
36 SolFin GmbH, Düsseldorf	75.10
37 WOWOBAU Wohnungsbaugesellschaft mbH, Munich (until September 30, 2016)	92.00

**The following company is included as an associate:**

Name of company	Shareholding (%)
1 AXA-ARAG Rechtsschutzversicherungsgesellschaft, Zurich/Switzerland	29.17

There were twelve Group companies that were not included in the consolidated financial statements (2015: 26) because these entities are not material, which means that their non-consolidation does not adversely affect the Group's net assets, financial position, or results of operations.

Janolaw AG, Sulzbach, in which the Group holds 25.1 percent of the shares, was not consolidated as an associate pursuant to section 311 (2) HGB because the entity does not prepare its financial statements in time and is not material to the Group's net assets, financial position, and results of operations.

**The following entities are not included in the consolidated financial statements in accordance with section 296 (2) and section 311 (2) HGB:**

Name of company	Shareholding (%)	Equity (€)	Net income for the year (€)
1 Agencia de Seguros ARAG S. A., Barcelona/Spain**	100.00	178,692.37	108,588.22
2 ARAG Services Spain & Portugal S. L., Barcelona/Spain*	100.00	361,825.63	18,698.82
3 ARAG-France S. A. R. L. Assistance et Règlement de Sinistres Automobiles et Généraux, Versailles/France	100.00	18,988.00	0.00
4 ATE Group Services Limited i. L., Bristol/United Kingdom*	100.00	1,233.72	0.00
5 ATE Limited i. L. (dormant), Bristol/United Kingdom*	100.00	89,043.33	0.00
6 COLUMBUS Immobilien Fonds XVI GmbH & Co. KG, Munich*	54.31	3,960,116.96	-609,784.02
7 Easy2claim Limited, Bristol/United Kingdom	100.00	1.17	0.00
8 JuroDirect B. V., Maastricht/Netherlands* (since June 28, 2016: Jurofoon B. V.)	100.00	508,375.00	-300,674.00
9 Jurofoon B. V., Maastricht/Netherlands* (until June 28, 2016)	100.00	789,250.00	87,731.00
10 Juronet B. V., Maastricht/Netherlands* (until June 28, 2016)	100.00	-612,363.00	-292,745.00
11 Prinzregent Vermögensverwaltungs-GmbH, Munich	92.00	33,518.09	672.63
12 VIF Gesellschaft für Versicherungsvermittlung mit beschränkter Haftung, Düsseldorf	100.00	247,808.87	216,262.43

\* Figures from the financial statements for the year ended December 31, 2015

\*\* Figures from the financial statements for the year ended December 31, 2014

**Procedures of consolidation**

The consolidated financial statements are prepared on the basis of the single-entity financial statements of the Group companies. The financial year covered the period January 1 to December 31, 2016 and was identical to the financial years of the consolidated companies.

Up to and including 2010, the accounting for subsidiaries in consolidated financial statements was based on the carrying amount method; the revaluation method used in subsequent years involved subtracting the equity attributable to the Group at the time of initial

consolidation from the cost of the equity investments in the consolidated subsidiaries. Where subtracting the equity attributable to the Group at the time of initial consolidation from the cost resulted in a positive difference, the carrying amounts of assets of the relevant subsidiaries were written up accordingly if there was the flexibility to do so in their valuation. Where there was no further scope to do so, the remaining amount was recognized as goodwill and amortized over its estimated useful life.

- 1** In the case of subsidiaries that were already included in the consolidated financial statements in 1989 in accordance with section 27 EGHGB or in cases where negative goodwill had arisen on acquisition that had affected the financial statements of the parent company in previous years, there was an offsetting against revenue reserves in earlier years. Goodwill amounts on initial consolidation have not been offset against revenue reserves since 2010 because this is no longer permitted under section 301 (3) HGB and German accounting standard (GAS) 4.84 et seq. (now: GAS 23).

On deconsolidation of a subsidiary, the income from the disposal is offset against the consolidated (residual) carrying amounts and the assets and liabilities attributable to that company. The share of non-controlling interests in the deconsolidated entity is derecognized in consolidated equity. A subsidiary is deconsolidated when the majority shareholders of the Group cease to have control pursuant to section 290 (2) HGB over the subsidiary. The investments in associates are recognized at the proportion of equity attributable to the Group or at historical cost to the Group pursuant to section 312 HGB. On initial application, the equity method is based on the values at the time of acquisition or at the time of preparation of the first annual financial statements after the acquisition where interim financial statements are not available. The different valuation of the assets and liabilities in the associates' financial statements compared with the valuation under commercial law is not adjusted for the purpose of applying the equity method.

Intercompany profit that is required to be eliminated is deducted from the carrying amounts of the affected assets and recognized in the income statement, provided that, overall, the amounts concerned are material to presenting a true and fair view of the net assets, financial position, and results of operations. The option pursuant to section 341j (2) HGB is generally utilized where the intercompany profit forms the basis for policyholder claims.

Group companies' receivables from, and liabilities to, other Group companies are offset against each other.

Consolidated entities' revenue from the provision of goods and services to other consolidated entities is offset against the associated expenses incurred by the providing entity unless the recipient is an insurance company.

Consolidated insurance companies' brokerage services provided to other consolidated insurance companies are performed on the basis of arm's-length terms and conditions that are typical in the market. Consolidation of commission resulting from brokerage and of goods and services provided by other Group companies to Group insurance companies is performed at the level of the providing entity by offsetting them against the related expenses.

### Currency translation

Balance sheets prepared in foreign currencies are translated into euros at the middle spot rate as of the balance sheet date in accordance with the balance-sheet-date principle. Amounts in the income statement that are recognized for the period are translated at an average of the month-end exchange rates. An amount of €1,265,468.93, representing the proportion attributable to the Group of the difference between the equity translated at the historical exchange rate and the equity translated at the closing rate, was recognized directly in equity under revenue reserves.

### Recognition, valuation, and presentation methods

The consolidated balance sheet and consolidated income statement are presented on the basis of the financial statement forms prescribed by the RechVersV.

Because the Group has multiple lines of business, the line item 'Land held for sale and other inventories of non-insurance companies' had to be added to the balance sheet and the items 'Revenue of non-insurance companies' and 'Cost of goods and services provided by non-insurance companies to generate revenue' had to be added to the income statement.

- 2 Goodwill** results partly from accounting for subsidiaries in consolidated financial statements and partly from acquisitions.

In accordance with GAS 4 no. 31 (now: GAS 23 no. 115), the amortization period is defined on the basis of the estimated useful life. For insurance companies, this is assumed to be 15 years (portfolio value); for other companies it is estimated on a case-by-case basis (up to five years). Goodwill with a remaining useful life of more than five years amounted to €10.3 million as of December 31, 2016. The useful life was originally set at 15 years because the goodwill was assumed to be part of the insurance portfolio. Experience shows that this fluctuates by between approximately 6 and 7 percent per year.

- 3 Miscellaneous intangible assets** are recognized at cost less straight-line amortization.

The carrying amount of €11,675,365.00 can be broken down as follows: €8,410,499.07 for software, €1,312,034.11 for leasehold improvements in business premises in Italy, €50,558.00 for industrial property rights, and €1,902,273.82 for goodwill arising on an acquisition in Spain. Software is essentially amortized over five years on a straight-line basis. Leasehold improvements are amortized over the remaining term of the leases using the straight-line method. The industrial property rights are not amortized (recognition at a fixed value). Goodwill is amortized over a period of six years. No write-downs were recognized in 2016.

- 4 Land and buildings** are valued at cost less depreciation and are written down in accordance with the discretionary principle of lower of cost or market value. It was not necessary to recognize any write-downs on land on the basis of expected permanent impairment in the reporting year. Land that is recognized as an investment is not encumbered by land charges used as collateral for liabilities to banks.

- 5 Shares in non-consolidated affiliated companies and miscellaneous equity investments** are carried at cost in accordance with section 253 (1) HGB, less write-downs resulting from long-term impairment. In the reporting year, write-downs of €2,060,282.67 were recognized on non-consolidated affiliated companies (2015: €10,002.00) and of €36,957.42 on miscellaneous equity investments (2015: €80,986.26). Reversals of write-downs pursuant to section 253 (5) HGB of €0.00 (2015: €184,121.49) were recognized on shares in non-consolidated affiliated companies and of €92,554.50 (2015: €3,691,410.00) on miscellaneous equity investments. **Investments in associates** are valued at their carrying amount at the time the shares were acquired or at the time of initial consolidation, plus or minus the pro-rata amount of changes in equity in subsequent years. The goodwill arising from using the equity method at the time of initial consolidation is already fully amortized. **Lending to non-consolidated affiliated companies** is recognized at the nominal amount. In the event of long-term impairment, the loans are written down to their fair value. As had been the case in 2015, no write-downs were recognized in the reporting year.
- 6 Equities, investment fund shares/units and other variable-yield securities** are generally valued at the lower of cost or market value as of the reporting date in accordance with section 341b (2) HGB in conjunction with section 253 (1), (4), and (5) HGB. The investment fund shares/units that were classified as fixed assets in previous years were valued using the discretionary principle of lower of cost or market value in accordance with section 253 (3) sentence 5 HGB. Write-downs are recognized only to the extent that the underlying impairment is considered to be long term. Correspondingly, reversals of write-downs are recognized only if the reversal is regarded as long term. As of December 31, 2016, the long-term market value was generally assumed to be the quoted market price – as it had been a year earlier. An exception was applied to the fixed-income institutional fund units, the market value of which was calculated as the total of the redemption amounts of the bonds contained in this fund, provided that they have an investment-grade rating. In the reporting year, write-downs amounting to €2,297,284.30 were recognized due to expected permanent impairment (2015: €42,268,143.41). Reversals of write-downs pursuant to section 253 (5) HGB were recognized in an amount of €24,991,398.96 in 2016 (2015: €657,926.58). The classification of institutional fund units for permanent use in business operations resulted in undisclosed liabilities of €2,640,468.07 (December 31, 2015: €13,085,405.19) due to write-downs not being recognized. As of December 31, 2016, the total fair value was not less than the carrying amount.
- 7 Bearer bonds and other fixed-income securities** are generally valued in accordance with the requirements for current assets pursuant to section 253 (1) sentence 1, (4), and (5) and section 256 HGB. In accordance with section 341b (2) second half-sentence HGB, some of the bonds and securities have been classified for permanent use in business operations. Due to this classification, which was carried out in previous years, undisclosed liabilities of €193,030.70 had arisen in respect of this subset of bonds and securities as of December 31, 2016 (December 31, 2015: €5,010,876.25) because no write-downs were recognized as the impairment was only temporary.

- 8 Sundry lending** comprises registered profit-participation certificates, miscellaneous loans, and prepayments for certificates of insurance. They are recognized at cost less repayments made.
- 9 Registered bonds** are accounted for at their nominal amount. Discounts are deferred using the straight-line method. Premiums are capitalized and recognized in income using the straight-line method over the term to maturity.
- 10 Loans secured by mortgages or land charges and fixed-income receivables, and other investments** are accounted for at cost or at their redemption amount. Write-downs pursuant to section 253 (3) sentence 5 HGB were recognized in an amount of €1,245,006.06 (2015: €0.00).
- 11 Investments for the account and at the risk of life insurance policyholders** are recognized at fair value. The gross provisions shown in line F. under equity and liabilities correspond to this fair value.
- 12 Bank deposits** are recognized at their nominal amount. In 2015, a current bank account with a balance of €6,441,969.84 had been pledged to Bank für Tirol und Vorarlberg AG as collateral for building loans.
- 13 Receivables** are generally recognized at their nominal amount. A general allowance for latent credit risk is deducted from receivables from policyholders and from trade receivables. Receivables from agents are reduced by specific allowances and a general allowance in the amount of the likely level of default.
- 14** In accordance with section 253 (1) sentence 1 HGB, **property and equipment** is recognized at cost and depreciated on a straight-line basis over the standard operating useful life.
- 15 Inventories** are determined by carrying out physical inventory checks. They are measured at cost.
- 16 Other assets** are recognized at their nominal amount. Tax credits pursuant to section 37 (5) of the German Corporation Tax Act (KStG) are valued at present value on the basis of a discount rate of 4.5 percent.
- 17 Prepaid expenses and accrued income** mainly consist of accrued rights to interest that are not yet due in respect of the income period before the balance sheet date and of cash payments expensed after the balance sheet date. This line item also includes an amount of €4,463,554.30 (December 31, 2015: €4,934,964.10) stemming from the difference pursuant to section 341c (2) sentence 2 HGB.
- 18 Deferred tax assets** include the likely tax benefit in subsequent financial years in the amount of the current or future income tax rates if their recognition is sufficiently certain. If valuation adjustments required to ensure consistent valuation in the consolidated financial statements arise between the carrying amounts in the HGB financial statements and those in the tax base because of temporary differences between the HGB financial statements and the tax base reported in single-entity financial statements and if differences arise because of consolidation activities, and these differences are expected to reverse in subsequent years, deferred taxes are recognized in respect of these valuation adjustments and differences using separate entity-specific tax rates. This also includes differences for

which the timing of the reversal is not yet precisely known or depends on action by the entity concerned, and differences that would only reverse in the event of any liquidation. Deferred tax assets have not been recognized for tax loss carryforwards. Differences are only recognized if their elimination in subsequent years is likely to lead to a decrease in the future tax expense as a result of a reduction in taxable income or a decline in effects from deferred tax liabilities. After the five-year forecast period has ended, differences that are likely to still not have been eliminated will be subjected to an individual, country-specific markdown if there are net deferred tax assets in order to take account of future imponderables that go beyond entity-specific planning and changes in future tax law. In 2016, €24.7 million of the amount resulting from expected reversal effects impacting on the basis of tax assessment in Germany was derecognized in the income statement.

- 19** The **excess of plan assets over pension liabilities** is the balance of pension obligations at present value and the fair value of the securities held to cover these liabilities.
- 20** **Subordinated liabilities** have been issued by way of private placement to strengthen the own funds used to determine the solvency ratio. The subordinated liabilities are recognized at their repayment amount (= settlement amount). The registered bonds are not negotiable in Germany on a regulated market within the meaning of section 2 (5) of the German Securities Trading Act (WpHG).
- 21** **Gross unearned premiums** for direct insurance business are calculated pro rata temporis on the basis of the premiums and cancellations posted, less the installment surcharges. In accordance with a circular from the German Federal Ministry of Finance (BMF) dated April 30, 1974, the non-transferable income components are deducted from the unearned premiums for the domestic parts of the business of the Group's insurance companies. A total of 85 percent of the commissions and other remuneration for agents is recognized as non-transferable income components. The capitalized portion of the acquisition costs are deducted from the unearned premiums for the non-German parts of the business. The reinsurers' share of the unearned premiums is determined in accordance with the contractual agreements.
- 22** The **life insurance actuarial reserves** – for sums insured and bonuses – for old policies are calculated in accordance with actuarial principles that have been communicated to the German Federal Financial Supervisory Authority (BaFin) in accordance with the business plan. The actuarial reserves are calculated on an individual policy basis using the prospective method with implied consideration of future costs. To this end, the following basis of calculation was used for individual endowment insurance policies and wealth-building life insurance policies (with a share of 32.2 percent of the total actuarial reserves): discount rates of 3 percent and 3.5 percent, zillmerizing of a maximum of 3.5 percent of the sums insured (exception: rates and charges with a higher death benefit), and mortality probabilities based on the ADSt 01/10 combined, ADSt 24/26 M, ADSt 60/62 mod. M, and ADSt 1986 mortality tables, separated into men and women.

The actuarial reserves for new premium-based policies are calculated on an individual policy basis using the prospective method (or retrospective method in the case of fund-linked products) with implied consideration of future administrative expenses. In the calculation of the surrender values and the actuarial reserve recognized on the balance sheet for the 2008 scale of rates and charges onward, the acquisition costs are allocated over five years in accordance with the provisions of the German Insurance Contracts Act (VVG). An explicit administrative expenses provision has been recognized to cover the premium-free periods of premium-free insurance policies – including, but not limited to, bonus sums insured and policies with a shortened period of premium payments. In accordance with section 143 of the German Insurance Supervision Act (VAG), BaFin has been notified of the basis of calculation used.

The individual endowment insurance policies (share of 24.0 percent of the total actuarial reserves) are calculated with a discount rate of 4 percent (94/95 and 98 scales of rates and charges), 3.25 percent (2000 scale of rates and charges), 2.75 percent (2004 scale of rates and charges), 2.25 percent (2007 and 2008 scale of rates and charges), 1.75 percent (2012 and 2013 scale of rates and charges), and 1.25 percent (2015 scale of rates and charges) and with a Zillmer rate of 3.3 percent of the sums insured (94/95 scale of rates and charges, with the exception of rates and charges with a higher death benefit) or a Zillmer rate of 4.0 percent of total premiums (1998, 2000, 2004, 2007, 2008, 2012, 2013 scales of rates and charges) or a Zillmer rate of 2.5 percent of total premiums (2015 scale of rates and charges onward), and mortality probabilities based on the DAV 1994 T mortality table, separated into men and women. The Company's own unisex tables based on the aforementioned DAV 1994 T mortality tables are used for the unisex scales of rates and charges from 2013 onward.

In the case of individual pension policies (share of 23.0 percent of the total actuarial reserves), the following basis of calculation was used until 2004: discount rate of 4 percent, 3.25 percent, or 2.75 percent, Zillmer rate of 3.3 percent of the lump sum (94/95 scale of rates and charges) or 4.0 percent of total premiums (1998, 2000, and 2004 scale of rates and charges), and mortality probabilities based on the DAV 1994 R mortality table, separated into men and women.

Analysis of changes in longevity by the German Actuarial Association (DAV) has found that the DAV 1994 R mortality table is no longer adequate for the recognition of reserves for pension insurance. On June 21, 2004, the DAV published guidance containing new mortality tables both for new business (DAV 2004 R mortality table) and for existing pension insurance policies (DAV 2004 R in-force business and R-B20 mortality tables).

Taking account of the company-specific probability of cancellations and lump sums, the actuarial reserve for all deferred and current pension insurance policies was also calculated as of December 31, 2016 using the new tables and a positive difference between the new and old actuarial reserves of €11.41 million was used to strengthen reserves.

The scale of rates and charges for pension insurance using the existing basis of calculation was closed for new business with effect from January 1, 2005. Since then, new pension insurance policies have been based solely on rates and charges using the latest basis of calculation: discount rate of 2.75 percent (2004 scale of rates and charges), 2.25 percent

(2007 and 2008 scales of rates and charges), 1.75 percent (2012 and 2013 scale of rates and charges), and 1.25 percent (2015 scale of rates and charges). The Company's own unisex tables based on the aforementioned DAV 2004 R mortality tables are used for the unisex scales of rates and charges from 2013 onward.

For supplementary disability insurance, the DAV 1997 I invalidity tables with a discount rate of 2.25 percent (2008 scale of rates and charges) or 1.75 percent (2012 scale of rates and charges) are used. The Company's own unisex disability tables based on the reinsurer's invalidity tables are used for the 2013 and 2014 unisex scales of rates and charges with a discount rate of 1.75 percent and for the 2015 scale of rates and charges with a discount rate of 1.25 percent.

In accordance with the German Regulation on the Principles Underlying the Calculation of the Premium Reserve (DeckRV), an additional actuarial reserve (supplementary change-in-discount-rate reserve) was recognized for the rates and charges whose guaranteed interest rate is above the reference rate for 2016 of 2.54 percent for new policies (2015: 2.88 percent) and 2.43 percent for old policies (2015: 2.75 percent). The total amount of this supplementary change-in-discount-rate reserve is €186.3 million (2015: €126.6 million); the increase in 2016 was €59.7 million (2015: €35.9 million).

For the supplementary disability insurance policies with an older basis of calculation, which have been closed for new business, a control calculation was carried out using the current basis of calculation from the German Actuarial Association. This revealed a need to add €0.5 million to reserves.

If claims against policyholders for acquisition cost loadings that have not yet been paid cannot be offset against the actuarial reserve, the claims are recognized in line item D. I. no. 1 b after deduction of general allowances for expected defaults.

The **actuarial reserve for health insurance** is calculated in accordance with actuarial principles defined in the technical basis of calculation individually for each insurance policy, applying the underlying data from the insurance policy in question. The transfer amounts contained in the actuarial reserve have been determined in accordance with section 14 of the German Regulation on the Supervision of Business Activities in Private Health Insurance (KVAV). The average discount rate is 3.14 percent.

The components of premiums from anticipated premium-free children's accident insurance policies are added to the **children's accident actuarial reserves**. The calculation is carried out using mathematical principles in accordance with the underwriting business plan.

**23** The **provision for outstanding claims** in relation to direct casualty and property insurance business is recognized separately by event year for claims reported in the financial year concerned and for anticipated claims that are reported after the balance sheet date. In addition, a provision for claim settlement expenses has been recognized pursuant to section 341g (1) HGB (for domestic parts of the business of the Group's insurance companies according to the coordinated regulations issued by the German federal states on February 2, 1973). Recourse claims that are expected to be recovered in the next year are deducted from the property insurance companies' claims provision.

The provision for outstanding claims in the inward reinsurance business is recognized in accordance with the information provided by the primary insurer. The provision for outstanding claims in connection with the inward reinsurance business from primary insurers in the United Kingdom is determined on the basis of past experience and statistics produced by the Group's own claims settlement company and is supplemented with additions for expected utilizations based on the Group's own empirical records. The proportions relating to outward reinsurance business are calculated in accordance with the stipulations in the reinsurance treaties.

Technical interest income is calculated at 1.25 percent of the arithmetic mean of the opening and closing balances of the actuarial reserve and the benefit reserves for annuities in the casualty and property insurance segment.

The provision for claims that have occurred by the balance sheet date but are **still outstanding and buybacks in life insurance** has been recognized on the basis of the premiums that are likely to be paid. A provision for outstanding claims has been recognized on the basis of empirical values for claims that occurred in 2016 but had not been reported by the time the balance sheet was prepared (IBNR claims).

A provision in the amount of the expenses that are likely to be incurred by settling these insurance benefits after the balance sheet date has also been recognized, taking the tax rules into consideration.

In accordance with rulings by the German Federal Court of Justice (BGH) dated October 12, 2005 and July 29, 2012, the actuarial reserve was increased by an additional lump sum of €2.4 million for the affected premium-free policies.

The provision for claims that had occurred by the balance sheet date but were **still outstanding in health insurance** was recognized on the basis of the claims payments in the reporting year in respect of previous years, taking a volume increase into consideration. One-off items that had not occurred in previous years were taken into account separately. The expenses that are likely to be incurred after the balance sheet date for settling claims from previous years were determined in accordance with the tax rules pursuant to section 341g (1) HGB on the basis of coordinated regulations issued by the German federal states on February 2, 1973.

**24** The **equalization provision** is recognized for the European business area (excluding Norway, Sweden, and Denmark) in accordance with section 341h HGB in conjunction with section 29 RechVersV. The equalization provision for the US, Canada, Norway, Sweden, and Denmark territories is calculated, where required, according to local regulatory rules.

**25** The **cancellation provision** reported under miscellaneous technical provisions to cover the discontinuation or reduction of technical risk is recognized in the amount of the estimated requirement. The **provision for expected losses** is recognized in accordance with section 31 (1) no. 2 RechVersV. To this end, the policies already sold in the loss-making insurance segments had been examined in 2015 as part of multi-year planning. The amount of the loss then expected was added to the provision for expected losses. In 2016, this provision was increased again in the life insurance segment in view of ARAG Lebensversicherungs-AG's earnings and the change in the value of recognized net assets resulting from the intention to sell and the purchase consideration already negotiated. The recognized amount includes a provision for the life insurance segment of €14,800,849.00.

**26** In accordance with standard international practice, **the provisions for pensions and other post-employment benefits** are calculated using the projected unit credit (PUC) method and applying section 253 (1) sentence 2 HGB on the basis of the 2005G mortality tables published by Professor Klaus Heubeck or local mortality tables that accurately reflect life expectancy. In addition to current circumstances, future trends in salaries, pensions, and staff turnover are taken into account. In accordance with section 253 (2) sentence 2 HGB, the discount rate used is the average interest rate for the past ten years published by Deutsche Bundesbank in accordance with the Regulation on the Discounting of Provisions (RückAbzinsV) for an assumed residual maturity of 15 years. Reflecting the statutory discount rate in force at the time, the average interest rate for the past seven years had been used in 2015. As a result of using a ten-year instead of a seven-year discount rate, the provision for pensions and other post-employment benefits decreased by €23,137,082.00 as of December 31, 2016.

The following actuarial parameters were used to calculate the obligations: pension age: earliest possible age under the Pension Age Reform Act (RVAGAnpG) in Germany, in accordance with individual agreements in Austria, 65 years in Spain; annual increase in salaries: 2.5 percent; annual increase in pension benefits: 1.75 percent (Spain: 2.5 percent); discount rate: 4.01 percent (discount rate pursuant to section 253 (2) sentence 2 HGB, ten-year average) and 3.24 percent (seven-year average, 2015: 3.89 percent).

The level of staff turnover taken into account reflects the generally observable age-dependent average for the industry (1.5 percent or sliding scale linked to age) and has only a minor impact on the settlement value.

The one-off increase arising under the valuation rules in section 253 (1) sentence 2 and (2) HGB (in the version based on the German Accounting Law Modernization Act (BilMoG)) amounts to €17,524,490.00. Of this amount, €15,927,915.00 had been added to the provision for pensions and other post-employment benefits by December 31, 2016, which means that a further €1,596,575.00 (December 31, 2015: €1,863,419.00) still needs to be added to the provision by no later than December 31, 2024 in accordance with section 67 (1) EGHGB.

Since 2010, assets that are protected from the claims of all other creditors and are used solely to settle liabilities arising from pension obligations have been offset against the obligation. This line item is therefore calculated as follows:

#### **Net provisions for pensions and other post-employment benefits**

(€)	Dec. 31, 2016	Dec. 31, 2015
Amount required to settle the vested entitlements	239,075,495.46	246,941,568.00
Netted assets (fair value)	- 6,667,883.10	- 5,985,040.74
Not yet added in accordance with section 67 (1) EGHGB	- 1,596,575.00	- 1,863,419.00
<b>Amount reported on the balance sheet</b>	<b>230,811,037.36</b>	<b>239,093,108.26</b>

In 2016, interest income of €106,127.02 (2015: €117,297.38) on the plan assets was offset in the income statement against the interest cost arising from the addition to the obligation. The option pursuant to section 28 (1) EGHGB, which permits provisions for pensions and other post-employment benefits not to be recognized for legacy entitlements, has not been exercised.

**27** The **provision for early retirement obligations** is recognized for those persons with whom individual contractual agreements have been reached. The provisions are calculated using actuarial principles. The probability of utilization is estimated individually.

In 2016, a **provision in accordance with the pre-retirement part-time employment agreement** for the private insurance industry dated June 11, 1997 and in accordance with the Accounting Principle issued by the Main Technical Committee of the Institute of Public Auditors in Germany (IDW AcP HFA 3) dated November 18, 1998 was recognized on the basis of a discount rate of 3.24 percent for matching maturities. In the case of deferred beneficiaries with whom a specific agreement has not yet been reached, the probability of their making use of the early retirement arrangements and natural employee attrition were taken into account. Credit balances on employee working hours accounts models are protected against insolvency in accordance with section 8a of the German Pre-Retirement Part-Time Employment Act (AltTZG) by means of a fixed liability guarantee from a German commercial bank.

The **undry provisions** and the **provisions for taxes** are recognized in the amount that is necessary to settle the obligation according to prudent business practice. A **long-service provision** was recognized in the year under review for long-service awards to be paid to employees. The provision was calculated using the projected unit credit method taking into account death rates in accordance with the 2005G mortality tables published by Professor Klaus Heubeck and applying a discount rate of 3.24 percent. The calculation also included staff turnover at an average rate of 1.5 percent and salary increases at a rate of 2.5 percent. The earliest possible pension age under the RVAGAnpG was selected as the final age.

**28** **Deposits received from reinsurers** and **other liabilities** are recognized at their settlement value. The residual maturity is less than one year in each case.

**29** The **liabilities from direct insurance business** and **liabilities from reinsurance business** are valued at their settlement value (nominal amount). The residual maturity is less than one year in each case.

**Liabilities with a residual maturity of more than five years** consisting of life insurance premium deposits amounted to €620,726.50 (December 31, 2015: €833,563.61).

**30 Liabilities to banks** in 2015 had predominantly arisen in respect of the real estate development business and had a residual maturity of less than five years. They were valued at their settlement value and were collateralized in an amount of €32,280,674.42 by mortgages on the land held for sale, by assignments of the purchase price, and by the pledging of bank accounts. As the real estate development company ceased to be an affiliate of the Group, there are no longer any liabilities to banks.

**31 Deferred income and accrued expenses** contain differences pursuant to section 341c (2) sentence 1 HGB of €13,544,647.63 (December 31, 2015: €14,079,205.28).

### **32 Consolidated equity**

Consolidated equity is presented in detail on pages 96 and 97 in accordance with GAS 7. Equity generated from Group earnings is shown as the portion of consolidated equity recognized from net profit for the reporting year or earlier financial years. It comprises revenue reserves, the profit or loss carried forward, and net income for the year and is broken down into controlling interests and non-controlling interests that have a direct or indirect equity investment in the subsidiaries included in the consolidated financial statements.

Changes in the Group's equity during the financial year that, according to commercial-law accounting principles and the rules of the German Accounting Standards Committee (GASC), must not be recognized in the income statement and that do not relate to incoming and outgoing payments at the level of the shareholders are shown in other comprehensive income.

The subscribed capital of the Group's parent company amounts to €200,000,000.00. It is divided into 200,000 no-par-value shares. All of the shares are registered.

The subscribed capital is fully paid up.

### Associates

The total goodwill arising on the consolidation of associates using the equity method amounted to €0.00 as of December 31, 2016 (December 31, 2015: €0.00). Accordingly, no amortization or write-downs were recognized on the goodwill of associates in 2016.

The financial statements of the sole associate can be summarized as follows:

#### AXA-ARAG Rechtsschutzversicherung

<i>(CHF '000, in accordance with Swiss accounting law)</i>	<b>2016</b>	<b>2015</b>
A. Investments	208,499	210,820
B. Receivables	31,570	15,871
C. Miscellaneous assets	13,671	13,574
D. Prepaid expenses and accrued income	0	0
<b>Total assets as of Dec. 31</b>	<b>253,740</b>	<b>240,265</b>
A. Equity	49,678	47,154
B. Technical provisions	174,607	167,146
C. Other provisions	80	80
D. Liabilities	29,375	25,885
E. Deferred income and accrued expenses	0	0
<b>Total equity and liabilities as of Dec. 31</b>	<b>253,740</b>	<b>240,265</b>
I. Underwriting result	14,417	12,849
II. Gains and losses on investments	4,215	3,585
III. Other net income/expense	-304	-346
IV. Tax expense	-3,805	-3,349
<b>Net income for the year</b>	<b>14,523</b>	<b>12,739</b>

## 33 II. Source of Insurance Business by Premiums Written

Country/source (€'000)	Direct insurance business				Inward reinsurance business		Total business
	Legal insurance	Casualty and property insurance	Health insurance	Life insurance	Legal insurance	Casualty and property insurance	
Germany	329,272	204,492	356,873	213,694		165	1,104,496
Netherlands	91,294				48,847		140,141
Austria	58,091						58,091
USA	80,703				7,396		88,099
Spain	47,306	46,704			21,274	9,805	125,089
Italy	26,321	4,426			87,341	331	118,419
Belgium	23,180				471		23,651
Norway	36,112						36,112
Greece	5,003				42		5,045
Slovenia	2,183						2,183
Portugal	448	188			182		818
Sweden	4,004						4,004
Denmark	57						57
UK*	1,295				22,199		23,494
<b>Total</b>	<b>705,269</b>	<b>255,810</b>	<b>356,873</b>	<b>213,694</b>	<b>187,752</b>	<b>10,301</b>	<b>1,729,699</b>

\* The reinsurance business involving risk in the UK is underwritten by ARAG SE in Düsseldorf.

## 34 III. Changes in Asset Items A., B. I. to IV. in 2016

## Changes in asset items

(€'000)	Carrying amount as of Jan. 1, 2016	Additions	Additions/ disposals in basis of consolidation	Reclassifications
<b>A. Intangible assets</b>				
1. Purchased goodwill	19,805	0	0	0
2. Miscellaneous intangible assets	12,490	4,092	-34	0
<b>Total for A.</b>	<b>32,296</b>	<b>4,092</b>	<b>-34</b>	<b>0</b>
<b>B. I. Land, land rights and buildings, including buildings on third-party land</b>	<b>243,222</b>	<b>1,195</b>	<b>0</b>	<b>0</b>
<b>B. II. Investments in affiliated companies and equity investments</b>				
1. Shares in affiliated companies	3,641	410	-211	0
2. Lending to affiliated companies	221	0	0	0
3. Equity investments	31,876	3,951	-180	0
4. Lending to long-term investees and investors	0	0	0	0
<b>Total for B. II.</b>	<b>35,738</b>	<b>4,361</b>	<b>-391</b>	<b>0</b>
<b>B. III. Miscellaneous investments</b>				
1. Equities, investment fund shares/units, and other variable-yield securities	2,330,465	120,018	0	3,959
2. Bearer bonds and other fixed-income securities	1,428,049	339,987	0	-3,959
3. Loans secured by mortgages or land charges and fixed-income receivables	114,118	144	5,810	0
4. Miscellaneous lending				
a) Registered bonds	1,050,056	68,000	0	0
b) Promissory notes and loans	651,100	77,000	0	0
c) Loans and prepayments for certificates of insurance	49,050	2,912	0	0
d) Sundry lending	4,379	57	3,400	0
5. Bank deposits	155,089	43,929	0	0
6. Other investments	25,839	18,088	0	0
<b>Total for B. III.</b>	<b>5,808,146</b>	<b>670,135</b>	<b>9,209</b>	<b>0</b>
<b>Total for B. I. to B. III.</b>	<b>6,087,106</b>	<b>675,692</b>	<b>8,818</b>	<b>0</b>
<b>B. IV. Deposits with ceding insurers</b>	<b>36,149</b>	<b>11,547</b>	<b>0</b>	<b>0</b>
<b>Total for investments B. I. to B. IV.</b>	<b>6,123,255</b>	<b>687,238</b>	<b>8,818</b>	<b>0</b>

Land, land rights and buildings on third-party land with a carrying amount of €136,240,231.30 are used for the business operations of the Group's insurance companies.

Disposals	Exchange-rate adjustments	Reversals of write-downs	Write-downs	Carrying amount as of Dec. 31, 2016	Fair value pursuant to sec. 54 RechVersV	Hidden reserves
0	52	0	3,410	16,447		
46	1	0	4,829	11,675		
<b>46</b>	<b>53</b>	<b>0</b>	<b>8,239</b>	<b>28,122</b>		
<b>1,238</b>	<b>0</b>	<b>0</b>	<b>6,086</b>	<b>237,093</b>	<b>381,183</b>	<b>144,090</b>
330	0	0	2,060	1,449	3,809	2,359
221	0	0	0	0	0	0
16,838	168	93	37	19,033	50,404	31,371
0	0	33	0	33	33	0
<b>17,389</b>	<b>168</b>	<b>125</b>	<b>2,097</b>	<b>20,514</b>	<b>54,245</b>	<b>33,731</b>
45,554	649	24,991	2,297	2,432,231	2,511,413	79,182
122,295	4,678	6,000	9,647	1,642,814	1,811,308	168,494
30,026	0	0	1,245	88,800	98,510	9,710
86,500	0	0	0	1,031,556	1,247,909	216,353
30,309	0	0	0	697,791	815,961	118,169
8,034	0	0	0	43,928	43,928	0
1,037	0	0	0	6,798	6,798	0
0	-3,456	0	0	195,562	195,562	0
1,809	0	0	0	42,119	47,871	5,752
<b>325,564</b>	<b>1,871</b>	<b>30,992</b>	<b>13,189</b>	<b>6,181,600</b>	<b>6,779,261</b>	<b>597,661</b>
<b>344,191</b>	<b>2,039</b>	<b>31,117</b>	<b>21,373</b>	<b>6,439,207</b>	<b>7,214,689</b>	<b>775,482</b>
<b>3,306</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>44,389</b>	<b>44,389</b>	<b>0</b>
<b>347,498</b>	<b>2,039</b>	<b>31,117</b>	<b>21,373</b>	<b>6,483,596</b>	<b>7,259,078</b>	<b>775,482</b>

## IV. Other Disclosures

### Investment fund disclosures

The portfolio of investments contains the following investment funds, of which more than 10 percent is held by the Group:

#### Institutional funds

Name	Type of fund	Investment objective	Carrying amount as of Dec. 31, 2016	Market value as of Dec. 31, 2016	Difference	Dividend in 2016	Redemption
			(€)	(€)	(€)	(€)	
ADRERENT	Fixed-income fund	Increased income	74,819,280.17	78,600,781.78	3,781,501.61	1,491,437.30	At any time
ATRI	Fixed-income fund	Increased income	149,919,473.82	149,772,293.97	-147,179.85	3,667,674.60	At any time
ARRE	Mixed fund	Increased income	247,061,291.12	257,235,310.16	10,174,019.04	6,517,812.07	At any time
ARI 1	Fixed-income fund	Increased income	283,248,547.47	283,248,547.47	0.00	13,808,747.58	At any time
ALLTIRENT	Fixed-income fund	Increased income	67,136,696.63	75,525,713.66	8,389,017.03	1,480,493.04	At any time
ALLTRI	Mixed fund	Increased income	123,007,017.54	139,346,482.08	16,339,464.54	3,403,141.28	At any time
ADZ	Fixed-income fund	Increased income	121,570,917.88	121,570,917.88	0.00	2,255,374.88	At any time
EMA	Equity fund	Increased income	62,972,405.56	63,094,367.96	121,962.40	2,445,021.60	At any time
AKR	Fixed-income fund	Increased income	259,824,509.85	262,702,984.97	2,878,475.12	6,530,584.00	At any time
BORGIA	Fixed-income fund	Increased income	207,348,710.53	205,884,863.06	-1,463,847.47	5,374,874.59	At any time
ALP	Fixed-income fund	Increased income	110,262,339.65	109,232,898.90	-1,029,440.75	3,567,754.94	At any time
ALF 1	Mixed fund	Increased income	169,005,401.09	169,005,401.09	0.00	5,916,886.60	At any time
ALM	Fixed-income fund	Increased income	207,848,945.50	207,848,945.50	0.00	3,974,089.28	At any time
AAF	Equity fund	Increased income	118,509,073.96	131,345,514.56	12,836,440.60	3,019,160.45	At any time
VM Sterntaler	Mixed fund	Increased income	4,938,732.00	6,786,018.00	1,847,286.00	100,362.89	At any time
SIVE Fonds INKA	Equity fund	Increased income	104,557,698.88	120,784,384.41	16,226,685.53	4,100,199.12	At any time
			<b>2,312,031,041.65</b>	<b>2,381,985,425.45</b>	<b>69,954,383.80</b>	<b>67,653,614.22</b>	

The investment objectives of the funds – which can be traded ahead of a stock market trading day – are based on the relevant benchmarks derived from the strategic investment structure. The Group made use of the option to select the discretionary principle of lower of cost or market value in accordance with section 341b (2) second half-sentence HGB for those institutional funds that are intended to be used permanently as part of the working capital of the Group. By classifying the listed funds as fixed assets, undisclosed liabilities of €2,640,468.07 were created (December 31, 2015: €12,709,193.81). Reversals of write-downs pursuant to section 253 (5) HGB were recognized on these funds in an amount of €24,516,193.53 in 2016 (2015: €513,833.04).

BaFin and the German Insurance Association (GDV) jointly specify the principles for determining the fair value pursuant to section 253 (3) sentence 5 HGB. These principles are followed when valuing fixed assets in accordance with the requirements.

### 35 Deferred taxes disclosures

The recognized deferred taxes arise from the differences between the HGB financial statements and the tax base. They relate to the following items:

#### Balance sheet items

(€'000)	Deferred taxes as of Dec. 31, 2016	Deferred taxes as of Dec. 31, 2015
Intangible assets	492	475
Investments	4,753	7,850
Receivables	1,317	2,002
Miscellaneous assets	138	380
Prepaid expenses and accrued income	-265	-147
Technical provisions	12,143	33,712
Other provisions	5,023	7,001
Other liabilities	-14	-4,543
Deferred income and accrued expenses	0	0
Loss carryforwards	0	0
	<b>23,587</b>	<b>46,730</b>

Differences that would not be accompanied by sufficient taxable income at the time of their probable reversal or would not be offset by countervailing effects in deferred taxes were capped in 2015. In addition, individual markdowns were recognized to reflect the uncertainty of the impact on current taxes at the time of reversal. In 2016, the reversal effects were compared with the outcome of a simplified tax planning process. Where there was no impact on current taxes or the effects were not offset by circumstances that increased the deferred taxes at the time of reversal, the notional net deferred tax asset was written down. Deferred tax assets are not recognized on losses carried forward.

**36 Unrealized gains on investments**

The amount shown is the difference between the fair values at the start (or the cost) and the fair values at the end of the financial year of the investments for the account and at the risk of life insurance policyholders. A corresponding expense is contained in 'Change in sundry net technical provisions'.

**37 Net extraordinary income/expense**

The extraordinary income and expenses arise as a result of applying the transitional provisions of the BilMoG dated May 25, 2009 in section 67 (1) EGHGB for the valuation of defined benefit obligations and pre-retirement part-time working obligations.

**38 Income taxes**

The breakdown of income taxes in the income statement is as follows:

	2016		2015	
	(%)	(€)	(%)	(€)
Profit before tax (HGB financial statements)		86,772,308.39		66,467,425.37
<b>Expected income tax expense based on tax rate</b>	31.20	<b>27,072,960.22</b>	31.20	<b>20,727,836.71</b>
Current taxes		19,183,873.05		41,217,868.90
Deferred taxes		23,041,647.08		-5,534,051.07
<b>Reported income tax expense</b>		<b>42,225,520.13</b>		<b>35,683,817.83</b>
Effective tax rate	48.67		53.68	
Miscellaneous taxes		1,428,818.86		1,556,283.66
<b>Tax expense reported in the income statement</b>		<b>43,654,338.99</b>		<b>37,240,101.49</b>

The discrepancy between the expected and effective tax expense essentially results from tax-exempt income and non-deductible expenses, the non-taxable net losses for the year of some Group companies, and the derecognition of temporary differences in net deferred tax assets.

### Miscellaneous financial commitments pursuant to section 285 no. 3 HGB

Rental and leasing agreements with varying terms for premises, vehicles, and office equipment as well as for the hardware and software used in a data center that have been concluded outside the insurance business give rise to total annual obligations that are of a standard magnitude for the industry.

The following unpaid contributions in respect of equity investments and private-equity fund structures are attributable to the Group:

### Unpaid contributions and obligations to pay in capital

Name of company	(€)
INVESCO Beteiligungsverwaltungs GmbH & Co. KG	243,380.86
RREEF Pan European Infrastructure Feeder GmbH & Co. KG	565,629.47
ACF V Growth Buy-out Europe GmbH & Co. KG	2,799,500.00
ACF VI Growth Buy-out Europe GmbH & Co. KG	6,243,000.00
AXA LBO Fund V Core	638,744.00
AXA LBO Fund V Supplementary	9,240.00
PAI Europe IV – Global SCSp	6,926,670.00
Bridgepoint Europe V	3,593,448.60
CROWN PREMIUM VI	15,660,000.00
Ardian LBO VI	8,610,603.11
Cube II	10,000,000.00
YIELCO I	17,825,000.00
FOYER-ARAG S. A., Luxembourg	24,788.00

None of the unpaid contributions have been called up. It would be reasonable to expect obligations to pay in capital to be called up by the investment funds (infrastructure and private-equity funds) in the near future. The sundry unpaid contributions will not be called up for the time being.

### Contingent liabilities

In accordance with section 221 et seq. VAG, the Group is a member of the protection fund for life insurers. On the basis of the German Regulation on the Financing of the Protection Fund for Life Insurers (SichLVFinV), the protection fund collects annual contributions of a maximum of 0.02 percent of the total net technical provisions until protection fund assets of 0.1 percent of the total net technical provisions have been reached. This does not create future obligations. The protection fund can also collect special contributions of a further 0.1 percent of the total net technical provisions, which equates to an obligation of €3,524,621.25 (December 31, 2015: €3,562,128.90). In addition, the Company has undertaken to provide the protection fund or, alternatively, Protektor Lebensversicherungs-AG with funding in the event that the protection fund's resources are not sufficient when restructuring is required. The obligation amounts to 1 percent of the total net technical provisions, taking into account the contributions already paid into the protection fund by that date. Including the above-mentioned obligations to make payments into the protection fund in relation to contributions, the total obligation as of the balance sheet date was €31,721,591.25 (December 31, 2015: €32,059,160.10).

The Group is also a member of the protection fund for providers of substitutive private health insurance. This protection fund can collect special contributions up to a maximum of 0.2 percent of the total net technical provisions for health insurance, which amounted to €3,671,688.31 as of the reporting date (December 31, 2015: €3,300,000.00).

### Auditor fees

The auditor of the consolidated financial statements is PricewaterhouseCoopers GmbH, Düsseldorf branch. The Group companies incurred expenses for auditor fees of €1,078,000.00 (2015: €828,000.00) for the audit of the annual financial statements, including the first audit of the Solvency II balance sheets. The expense for other consultancy or advisory services totaled €405,652.20 (2015: €258,088.92). Tax consultancy fees of €111,210.03 were paid (2015: €32,582.82). A standard amount of out-of-pocket expenses was reimbursed on top of the fees. As there is no entitlement to offset input VAT, the VAT on the auditor fees and out-of-pocket expenses is also recognized as an additional expense.

**39 Expenses for bonuses and rebates for own account**

(€)	2016	2015
Expenses for performance-based bonuses and rebates	70,241,816.83	57,600,293.78
Expenses for non-performance-based bonuses and rebates	1,240,544.04	35,032.24
<b>Total expenses</b>	<b>71,482,360.87</b>	<b>57,635,326.02</b>

**Commissions and other remuneration for insurance agents, staff costs**

(€)	2016	2015
1. Commissions of all types for insurance agents within the meaning of section 92 HGB for direct insurance business	249,971,181.09	233,372,206.26
2. Other remuneration for insurance agents within the meaning of section 92 HGB	16,302,558.54	17,374,773.42
3. Wages and salaries	241,577,391.59	233,141,209.35
4. Social security and other employee benefit expenses	39,084,775.63	37,652,695.78
5. Pension and other post-employment benefit expenses	8,269,863.90	30,976,499.53
<b>6. Total expenses</b>	<b>555,205,770.75</b>	<b>552,517,384.34</b>

**Average number of employees in 2016**

The Group's fully consolidated entities employed an average of 3,921 people in 2016 (2015: 3,757). As of December 31, 2016, the Group had a total of 4,053 employees (December 31, 2015: 3,870).

The insurance companies employed an average of 3,460 people (2015: 3,305). The average number of people employed by all of the administrative entities and service companies was 524 (2015: 511). In the German Group companies, an additional eight people were employed for the purpose of vocational training (2015: nine).

**Remuneration of the Supervisory Board and Management Board of ARAG Holding SE**

The expense for Supervisory Board remuneration in all Group companies came to €315,791.15.

In accordance with section 314 (3) HGB, the remuneration for the members of the parent company's Management Board from all Group companies is not disclosed. There are no current pensions or vested pension entitlements for former members of the Management Board and their surviving dependants.

## V. Report on Post-Balance Sheet Events

In the reporting year, the ARAG Group decided to no longer operate the life insurance business itself. Against a backdrop of persistently low interest rates, ARAG SE began to reorganize the ARAG Group structure and decided to sell its shares in ARAG Lebensversicherungs-AG to Frankfurter Leben-Gruppe. The sale of the shares is subject to approval by BaFin. As a result of the sale, the entire life insurance segment – including all business opportunities and all risks – will be removed from the ARAG Group. The Group's total assets will thus decrease by €2,901.2 million. Free cash flow will contract by around €7.2 million. The sale of the shares will cause insurance sales revenue to fall by approximately €215 million in the short term. It is not yet possible to definitively estimate what impact the sale of ARAG Lebensversicherungs-AG and the transfer of certain assets of ARAG Lebensversicherungs-AG to other Group companies will have on the Group's net profit because the effective date of the sale depends on BaFin's decision.

There were no events of particular importance between the end of the reporting year and the date of preparation of the consolidated financial statements. Business performance so far has been in line with expectations.

Düsseldorf, April 4, 2017

The Management Board

Dr. Dr. h. c. Paul-Otto Faßbender

Dr. Sven Wolf

## Consolidated Cash Flow Statement for 2016

### Cash flow statement

(€)	2016	2015
<b>Cash flows from operating activities</b>		
Profit for the period	43,117,969	29,227,324
Increase (+)/decrease (-) in technical provisions, net	231,467,598	215,299,677
Increase (-)/decrease (+) in deposits with ceding insurers and in receivables from reinsurance business	- 8,918,989	- 16,448,585
Increase (+)/decrease (-) in deposits from reinsurers and liabilities from reinsurance business	- 4,759,144	- 3,346,205
Increase (-)/decrease (+) in receivables from direct insurance business	8,885,401	13,107,328
Increase (+)/decrease (-) in liabilities from direct insurance business	17,450,770	- 4,090,040
Increase (-)/decrease (+) in miscellaneous receivables	29,174,788	- 3,549,031
Increase (+)/decrease (-) in miscellaneous liabilities	- 56,284,034	2,524,420
Change in miscellaneous balance sheet items not related to investing or financing activities	- 235,104,352	- 145,439,896
Other non-cash income and expenses, and adjustment of the profit/loss for the period	8,488,749	47,921,711
Gain (-)/loss (+) on the disposal of investments, property and equipment, and intangible fixed assets	- 41,799,734	- 39,120,877
Expenses for/income from extraordinary items	266,844	266,844
Current income tax expense/income	19,183,873	30,149,767
Cash receipts from extraordinary items	0	0
Cash payments for extraordinary items	0	0
Income taxes paid	- 2,161,192	- 35,494,866
<b>Cash flows from operating activities</b>	<b>9,008,548</b>	<b>91,007,572</b>
<b>Cash flows from investing activities</b>		
Proceeds from disposal of consolidated entities	11,000,000	0
Proceeds from disposal of property and equipment	269,493	1,098,724
Proceeds from disposal of intangible fixed assets	84,010	745,993
Payments to acquire property and equipment	- 5,703,229	- 7,186,656
Payments to acquire intangible fixed assets	- 4,077,130	- 8,759,187
Proceeds from disposal of investments related to fund-linked life insurance	0	0
Payments to acquire investments related to fund-linked life insurance	0	0
Cash receipts from extraordinary items	0	0
Cash payments for extraordinary items	0	0
<b>Cash flows from investing activities</b>	<b>1,573,144</b>	<b>- 14,101,126</b>
<b>Cash flows from financing activities</b>		
Proceeds from capital contributions by shareholders	0	0
Cash payments to shareholders from the redemption of shares	0	0
Cash receipts from extraordinary items	0	0
Cash payments for extraordinary items	0	0
Dividends paid	- 10,000,000	- 10,000,000
Proceeds (+)/cash payments (-) related to miscellaneous financing activities	0	- 50,000,000
<b>Cash flows from financing activities</b>	<b>- 10,000,000</b>	<b>- 60,000,000</b>
Net change in cash and cash equivalents	581,692	16,906,445
Effect on cash and cash equivalents of exchange rate movements and remeasurements	0	0
Effect on cash and cash equivalents of changes in the basis of consolidation	- 5,543,576	0
Cash and cash equivalents at beginning of period	155,312,016	138,405,571
<b>Cash and cash equivalents at end of period</b>	<b>150,350,132</b>	<b>155,312,016</b>

## 40 Statement of Changes in Equity

### Changes in the reporting year

(€)	Subscribed capital	Uncalled unpaid contributions	Equity generated from Group earnings	Adjustment items relating to currency translation	Equity reported on the consolidated balance sheet
<b>I. Parent company</b>					
Balance as of December 31, 2015	200,000,000.00	0.00	208,299,738.65	11,202,980.20	419,502,718.85
Issue of shares					0.00
Acquisition/retirement of treasury shares					0.00
Dividends paid			-10,000,000.00		-10,000,000.00
Changes in the basis of consolidation			0.00		0.00
Sundry changes			0.00	1,265,468.93	1,265,468.93
Net income for the year			42,804,068.63		42,804,068.63
Other comprehensive income					0.00
Total comprehensive income			42,804,068.63	0.00	42,804,068.63
<b>Balance as of December 31, 2016</b>	<b>200,000,000.00</b>	<b>0.00</b>	<b>241,103,807.28</b>	<b>12,468,449.13</b>	<b>453,572,256.41</b>
<b>II. Non-controlling interests</b>					
Balance as of December 31, 2015	0.00	0.00	6,966,237.23	27,894.68	6,994,131.91
Issue of shares					0.00
Acquisition/retirement of treasury shares					0.00
Dividends paid			-209,829.10		-209,829.10
Changes in the basis of consolidation			-1,222,509.70		-1,222,509.70
Sundry changes			2,266,139.97		2,266,139.97
Net income for the year			313,900.77		313,900.77
Other comprehensive income					0.00
Total comprehensive income			313,900.77		313,900.77
<b>Balance as of December 31, 2016</b>	<b>0.00</b>	<b>0.00</b>	<b>8,113,939.17</b>	<b>27,894.68</b>	<b>8,141,833.85</b>
<b>III. Consolidated equity</b>					
Balance as of December 31, 2015	200,000,000.00	0.00	215,265,975.88	11,230,874.88	426,496,850.76
Issue of shares			0.00		0.00
Acquisition/retirement of treasury shares					0.00
Dividends paid			-10,209,829.10		-10,209,829.10
Changes in the basis of consolidation			-1,222,509.70		-1,222,509.70
Sundry changes			2,266,139.97	1,265,468.93	3,531,608.90
Net income for the year			43,117,969.40		43,117,969.40
Other comprehensive income					0.00
Total comprehensive income			43,117,969.40		43,117,969.40
<b>Balance as of December 31, 2016</b>	<b>200,000,000.00</b>	<b>0.00</b>	<b>249,217,746.45</b>	<b>12,496,343.81</b>	<b>461,714,090.26</b>

## Changes in the previous year

(€)	Subscribed capital	Uncalled unpaid contributions	Equity generated from Group earnings	Adjustment items relating to currency translation	Equity reported on the consolidated balance sheet
<b>I. Parent company</b>					
Balance as of December 31, 2014	200,000,000.00	0.00	189,038,471.21	4,488,483.88	393,526,955.09
Issue of shares					0.00
Acquisition/retirement of treasury shares					0.00
Dividends paid			-10,000,000.00		-10,000,000.00
Changes in the basis of consolidation			0.00		0.00
Sundry changes			-0.01	6,714,496.32	6,714,496.31
Net income for the year			29,261,267.45		29,261,267.45
Other comprehensive income					0.00
Total comprehensive income			29,261,267.45	0.00	29,261,267.45
<b>Balance as of December 31, 2015</b>	<b>200,000,000.00</b>	<b>0.00</b>	<b>208,299,738.65</b>	<b>11,202,980.20</b>	<b>419,502,718.85</b>
<b>II. Non-controlling interests</b>					
Balance as of December 31, 2014	0.00	0.00	7,069,082.51	27,894.68	7,096,977.19
Issue of shares					0.00
Acquisition/retirement of treasury shares					0.00
Dividends paid			-173,901.71		-173,901.71
Changes in the basis of consolidation			0.00		0.00
Sundry changes			105,000.00		105,000.00
Net income for the year			-33,943.57		-33,943.57
Other comprehensive income					0.00
Total comprehensive income			-33,943.57		-33,943.57
<b>Balance as of December 31, 2015</b>	<b>0.00</b>	<b>0.00</b>	<b>6,966,237.23</b>	<b>27,894.68</b>	<b>6,994,131.91</b>
<b>III. Consolidated equity</b>					
Balance as of December 31, 2014	200,000,000.00	0.00	196,107,553.72	4,516,378.56	400,623,932.28
Issue of shares			0.00		0.00
Acquisition/retirement of treasury shares					0.00
Dividends paid			-10,173,901.71		-10,173,901.71
Changes in the basis of consolidation			0.00		0.00
Sundry changes			104,999.99	6,714,496.32	6,819,496.31
Net income for the year			29,227,323.88		29,227,323.88
Other comprehensive income					0.00
Total comprehensive income			29,227,323.88		29,227,323.88
<b>Balance as of December 31, 2015</b>	<b>200,000,000.00</b>	<b>0.00</b>	<b>215,265,975.88</b>	<b>11,230,874.88</b>	<b>426,496,850.76</b>

## Segment Reporting – Balance Sheet

	Legal insurance		Casualty and property insurance		Health insurance	
	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
(€'000)						
<b>A. Intangible assets</b>	<b>10,075</b>	<b>11,150</b>	<b>273</b>	<b>410</b>	<b>77</b>	<b>92</b>
<b>B. Investments</b>	<b>1,929,202</b>	<b>1,785,530</b>	<b>438,109</b>	<b>422,848</b>	<b>1,866,695</b>	<b>1,701,740</b>
I. Land and buildings, including buildings on third-party land	70,172	73,482	30,394	30,627	30,182	30,657
II. Investments in affiliated companies and equity investments	284,573	279,062	35,329	33,479	12,049	6,960
III. Miscellaneous investments	1,535,212	1,400,491	367,242	355,089	1,824,464	1,664,122
IV. Deposits with ceding insurers	39,245	32,496	5,144	3,653	0	0
<b>C. Investments for the account and at the risk of life insurance policyholders</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>D. Sundry segment assets</b>	<b>257,355</b>	<b>312,275</b>	<b>27,515</b>	<b>23,961</b>	<b>57,595</b>	<b>42,431</b>
<b>Total segment assets</b>	<b>2,196,631</b>	<b>2,108,956</b>	<b>465,898</b>	<b>447,218</b>	<b>1,924,368</b>	<b>1,744,263</b>
<b>A. Technical provisions</b>	<b>1,307,081</b>	<b>1,292,947</b>	<b>315,506</b>	<b>293,757</b>	<b>1,835,844</b>	<b>1,662,374</b>
I. Unearned premiums	195,537	194,633	44,479	40,528	14,396	13,979
II. Actuarial reserve	0	0	4	4	1,546,230	1,405,291
III. Provision for outstanding claims	1,109,502	1,096,831	224,113	219,335	58,483	51,006
IV. Provision for bonuses and rebates	0	0	0	0	216,526	191,841
V. Equalization provision	4,361	1,486	74,249	64,333	0	0
VI. Miscellaneous technical provisions	882	2,347	2,001	2,180	209	257
VII. Reinsurers' share of technical provisions	-3,202	-2,350	-29,340	-32,624	0	0
<b>B. Technical provisions in the life insurance business where the investment risk is borne by the insurance companies</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>C. Miscellaneous segment liabilities</b>	<b>358,993</b>	<b>332,307</b>	<b>47,057</b>	<b>50,973</b>	<b>19,176</b>	<b>22,630</b>
<b>Total segment liabilities</b>	<b>1,666,075</b>	<b>1,625,254</b>	<b>362,563</b>	<b>344,730</b>	<b>1,855,020</b>	<b>1,685,004</b>
<b>Equity*</b>						
<b>Total equity and liabilities</b>						

\* Consolidated equity including non-controlling interests and goodwill arising on consolidation

The segment reporting was largely adapted to German accounting standard GAS 3–20 of the German Accounting Standards Board (GASB). The segment data is presented after consolidation of internal transactions within each business line. Reconciliation with the figure for the Group is based on the amounts stated in the 'Consolidation' column. Gains and losses on investments are initially retained in the segments and not eliminated until the 'Consolidation' column.

The segmentation follows the internal organizational and management structure of the ARAG Group, which is based on strategic business lines. The segments chosen reflect the Group's risks and opportunities.

The strategic business lines are:

- Legal insurance
- Casualty and property insurance
- Life insurance
- Health insurance
- Services and asset management.

Life insurance		Services and asset management		Total		Consolidation		Group total	
Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
105	91	2,891	2,718	13,421	14,461	14,702	17,834	28,122	32,296
2,609,446	2,553,446	386,170	398,972	7,229,622	6,862,536	-746,025	-739,282	6,483,596	6,123,255
102,410	104,404	6,946	7,071	240,104	246,241	-3,011	-3,019	237,093	243,222
79,850	91,089	351,728	361,411	763,529	772,000	-743,015	-736,263	20,514	35,738
2,427,186	2,357,953	27,495	30,490	6,181,600	5,808,146	0	0	6,181,600	5,808,146
0	0	0	0	44,389	36,149	0	0	44,389	36,149
287,407	298,942	0	0	287,407	298,942	0	0	287,407	298,942
90,675	91,476	50,227	142,675	483,367	612,819	15,689	15,059	499,056	627,878
2,987,632	2,943,955	439,287	544,366	8,013,816	7,788,758	-715,635	-706,388	7,298,181	7,082,370
2,506,517	2,472,868	0	0	5,964,948	5,721,946	0	0	5,964,948	5,721,946
3,812	4,072	0	0	258,223	253,212	0	0	258,223	253,212
2,408,757	2,355,573	0	0	3,954,990	3,760,868	0	0	3,954,990	3,760,868
7,598	23,824	0	0	1,399,696	1,390,997	0	0	1,399,696	1,390,997
106,898	117,392	0	0	323,424	309,233	0	0	323,424	309,233
0	0	0	0	78,611	65,819	0	0	78,611	65,819
14,967	12,514	0	0	18,059	17,299	0	0	18,059	17,299
-35,514	-40,507	0	0	-68,056	-75,481	0	0	-68,056	-75,481
287,407	298,942	0	0	287,407	298,942	0	0	287,407	298,942
125,475	118,198	33,410	110,878	584,112	634,985	0	0	584,112	634,985
2,919,400	2,890,007	33,410	110,878	6,836,467	6,655,873	0	0	6,836,467	6,655,873
								461,714	426,497
								7,298,181	7,082,370

The service companies and asset management companies comprise the Group parent company and other intermediate holding companies that manage assets, including, but not limited to, a house-building company (until September 30, 2016), real-estate management companies, IT companies, and service companies that support the insurance business.

The life insurance segment also includes companies that provide services in the life insurance business line but are not insurance companies themselves.

Because deferred taxes are recognized in accordance with the temporary concept, the segment breakdown of the income statement now only goes as far as the 'Profit/loss before tax' line.

## Segment Reporting – Income Statement by Class of Insurance

(€'000)	Legal insurance		Casualty and property insurance		Health insurance	
	2016	2015	2016	2015	2016	2015
<b>Underwriting income</b>						
<b>Gross premiums written</b>	<b>893,021</b>	<b>841,697</b>	<b>266,110</b>	<b>246,648</b>	<b>356,873</b>	<b>347,450</b>
Direct insurance business	705,268	670,699	255,809	239,317	356,873	347,450
Inward reinsurance business	187,753	170,998	10,301	7,332	0	0
Reinsurance premiums ceded	-4,506	-3,897	-8,494	-7,436	-315	-15
Change in net unearned premiums	-242	-7,641	-3,948	-794	-417	-558
<b>Premiums earned for own account</b>	<b>888,274</b>	<b>830,158</b>	<b>253,667</b>	<b>238,418</b>	<b>356,141</b>	<b>346,878</b>
Premiums from the gross provision for bonuses and rebates	0	0	0	0	34,736	23,706
Investment income allocated to the underwriting account	0	313	634	614	74,491	63,164
Unrealized gains on investments	0	0	0	0	0	0
Miscellaneous underwriting income for own account	1,464	1,466	437	543	1,805	1,487
<b>Total underwriting income</b>	<b>889,738</b>	<b>831,938</b>	<b>254,738</b>	<b>239,575</b>	<b>467,173</b>	<b>435,235</b>
<b>Underwriting expenses</b>						
Claims incurred net of reinsurance	-440,048	-426,774	-138,908	-125,058	-202,796	-193,784
Change in sundry net technical provisions	-6	-242	180	-238	-140,891	-121,065
Expenses for bonuses and rebates	0	0	0	0	-68,891	-53,471
of which performance-based	0	0	0	0	-67,651	-53,436
of which non-performance-based	0	0	0	0	-1,241	-35
Unrealized losses on investments	0	0	0	0	0	0
Insurance business operating expenses	-383,334	-367,194	-101,894	-95,721	-38,203	-38,089
of which front-end fees	-90,394	-89,263	-35,242	-29,158	-29,649	-28,541
of which administrative expenses	-295,340	-279,424	-67,309	-66,979	-8,554	-9,554
of which reinsurers' share	2,400	1,493	656	416	0	6
Investment expenses allocated to the underwriting account	0	0	0	0	-6,958	-12,752
Miscellaneous underwriting expenses for own account	0	-11	-1,698	-1,709	-917	-1,525
<b>Total underwriting expenses</b>	<b>-823,388</b>	<b>-794,221</b>	<b>-242,320</b>	<b>-222,726</b>	<b>-458,655</b>	<b>-420,686</b>
<b>Subtotal</b>	<b>66,350</b>	<b>37,716</b>	<b>12,418</b>	<b>16,849</b>	<b>8,518</b>	<b>14,549</b>
Change in equalization provision and similar provisions	-2,875	-1,486	-9,916	-4,296	0	0
<b>Underwriting result for own account</b>	<b>63,475</b>	<b>36,230</b>	<b>2,502</b>	<b>12,553</b>	<b>8,518</b>	<b>14,549</b>
Income from investments	93,937	102,006	15,405	15,942	74,491	63,164
Expenses for investments	-19,012	-27,401	-4,156	-6,158	-6,958	-12,752
<b>Gains and losses on investments</b>	<b>74,925</b>	<b>74,604</b>	<b>11,249</b>	<b>9,784</b>	<b>67,534</b>	<b>50,412</b>
Gains and losses on investments assigned to the underwriting account	0	0	0	0	-67,534	-50,412
Revenue of non-insurance companies	0	0	0	0	0	0
Cost of goods and services provided by non-insurance companies to generate revenue	0	0	0	0	0	0
<b>Gross profit</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
Other income	18,720	17,371	3,513	836	1,870	499
Other expenses	-53,381	-58,502	-5,895	-6,697	-3,576	-3,908
<b>Other net income/expense</b>	<b>-34,661</b>	<b>-41,131</b>	<b>-2,383</b>	<b>-5,861</b>	<b>-1,705</b>	<b>-3,409</b>
<b>Profit/loss from ordinary activities</b>	<b>103,739</b>	<b>69,704</b>	<b>11,368</b>	<b>16,476</b>	<b>6,812</b>	<b>11,139</b>
<b>Net extraordinary income/expense</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Profit/loss before tax</b>	<b>103,739</b>	<b>69,704</b>	<b>11,368</b>	<b>16,476</b>	<b>6,812</b>	<b>11,139</b>
Tax expense						
<b>Net income for the year</b>						
of which non-controlling interests						

Life insurance		Services and asset management		Total		Consolidation		Group total	
2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
<b>213,694</b>	<b>220,263</b>	<b>0</b>	<b>0</b>	<b>1,729,698</b>	<b>1,656,058</b>	<b>0</b>	<b>0</b>	<b>1,729,698</b>	<b>1,656,058</b>
213,694	220,263	0	0	1,531,645	1,477,728	0	0	1,531,645	1,477,728
0	0	0	0	198,054	178,330	0	0	198,054	178,330
-5,566	-4,795	0	0	-18,881	-16,143	0	0	-18,881	-16,143
237	313	0	0	-4,371	-8,680	0	0	-4,371	-8,680
<b>208,365</b>	<b>215,781</b>	<b>0</b>	<b>0</b>	<b>1,706,447</b>	<b>1,631,235</b>	<b>0</b>	<b>0</b>	<b>1,706,447</b>	<b>1,631,235</b>
2,659	3,944	0	0	37,395	27,650	0	0	37,395	27,650
137,041	144,860	0	0	212,166	208,951	-2,322	-2,247	209,844	206,704
1,605	9,373	0	0	1,605	9,373	0	0	1,605	9,373
5,748	5,908	0	0	9,454	9,405	0	0	9,454	9,405
<b>355,418</b>	<b>379,866</b>	<b>0</b>	<b>0</b>	<b>1,967,067</b>	<b>1,886,614</b>	<b>-2,322</b>	<b>-2,247</b>	<b>1,964,745</b>	<b>1,884,367</b>
-233,127	-228,995	0	0	-1,014,879	-974,611	0	0	-1,014,879	-974,611
-45,868	-51,273	0	0	-186,586	-172,818	0	0	-186,586	-172,818
-2,591	-4,165	0	0	-71,482	-57,635	0	0	-71,482	-57,635
-2,591	-4,165	0	0	-70,242	-57,600	0	0	-70,242	-57,600
0	0	0	0	-1,241	-35	0	0	-1,241	-35
-7,278	-1,338	0	0	-7,278	-1,338	0	0	-7,278	-1,338
-23,043	-29,742	0	0	-546,474	-530,746	0	0	-546,474	-530,746
-17,362	-21,979	0	0	-172,646	-168,941	0	0	-172,646	-168,941
-7,234	-7,629	0	0	-378,437	-363,585	0	0	-378,437	-363,585
1,552	-135	0	0	4,609	1,780	0	0	4,609	1,780
-25,584	-35,026	0	0	-32,542	-47,778	0	0	-32,542	-47,778
-23,363	-24,302	0	0	-25,978	-27,548	0	0	-25,978	-27,548
<b>-360,855</b>	<b>-374,841</b>	<b>0</b>	<b>0</b>	<b>-1,885,218</b>	<b>-1,812,474</b>	<b>0</b>	<b>0</b>	<b>-1,885,218</b>	<b>-1,812,474</b>
<b>-5,437</b>	<b>5,025</b>	<b>0</b>	<b>0</b>	<b>81,849</b>	<b>74,140</b>	<b>-2,322</b>	<b>-2,247</b>	<b>79,527</b>	<b>71,893</b>
0	0	0	0	-12,792	-5,783	0	0	-12,792	-5,783
<b>-5,437</b>	<b>5,025</b>	<b>0</b>	<b>0</b>	<b>69,057</b>	<b>68,357</b>	<b>-2,322</b>	<b>-2,247</b>	<b>66,735</b>	<b>66,110</b>
137,041	144,860	29,844	30,872	350,718	356,844	-56,644	-64,432	294,075	292,412
-25,584	-35,026	-2,539	-405	-58,249	-81,743	4,196	374	-54,053	-81,370
<b>111,457</b>	<b>109,834</b>	<b>27,304</b>	<b>30,467</b>	<b>292,470</b>	<b>275,101</b>	<b>-52,448</b>	<b>-64,059</b>	<b>240,022</b>	<b>211,042</b>
-111,457	-109,834	0	0	-178,991	-160,246	2,322	2,247	-176,669	-157,999
0	0	98,002	108,492	98,002	108,492	-43,173	-41,852	54,830	66,640
0	0	-92,719	-103,890	-92,719	-103,890	43,173	41,852	-49,547	-62,038
<b>0</b>	<b>0</b>	<b>5,283</b>	<b>4,602</b>	<b>5,283</b>	<b>4,602</b>	<b>0</b>	<b>0</b>	<b>5,283</b>	<b>4,602</b>
4,406	3,165	745	1,952	29,254	23,823	0	657	29,254	24,480
-7,666	-5,066	-3,951	-4,207	-74,469	-78,380	-3,117	-3,120	-77,586	-81,501
<b>-3,259</b>	<b>-1,902</b>	<b>-3,206</b>	<b>-2,255</b>	<b>-45,215</b>	<b>-54,557</b>	<b>-3,117</b>	<b>-2,464</b>	<b>-48,332</b>	<b>-57,021</b>
<b>-8,697</b>	<b>3,124</b>	<b>29,381</b>	<b>32,814</b>	<b>142,603</b>	<b>133,257</b>	<b>-55,564</b>	<b>-66,522</b>	<b>87,039</b>	<b>66,734</b>
<b>-197</b>	<b>-197</b>	<b>-70</b>	<b>-70</b>	<b>-267</b>	<b>-267</b>	<b>0</b>	<b>0</b>	<b>-267</b>	<b>-267</b>
<b>-8,893</b>	<b>2,927</b>	<b>29,311</b>	<b>32,744</b>	<b>142,337</b>	<b>132,990</b>	<b>-55,564</b>	<b>-66,522</b>	<b>86,772</b>	<b>66,467</b>
								-43,654	-37,240
								<b>43,118</b>	<b>29,227</b>
								314	-34

## Segment Reporting – Income Statement by German and International Business

(€'000)	German	
	2016	2015
<b>Underwriting income</b>		
<b>Gross premiums written</b>	<b>1,126,696</b>	<b>1,095,468</b>
Direct insurance business	1,104,331	1,073,677
Inward reinsurance business	22,364	21,790
Reinsurance premiums ceded	-14,624	-12,515
Change in net unearned premiums	-6,269	-4,639
<b>Premiums earned for own account</b>	<b>1,105,803</b>	<b>1,078,314</b>
Premiums from the gross provision for bonuses and rebates	37,395	27,650
Investment income allocated to the underwriting account	212,166	208,637
Unrealized gains on investments	1,605	9,373
Miscellaneous underwriting income for own account	9,282	9,247
<b>Total underwriting income</b>	<b>1,366,251</b>	<b>1,333,222</b>
<b>Underwriting expenses</b>		
Claims incurred net of reinsurance	-754,140	-728,676
Change in sundry net technical provisions	-186,612	-172,600
Expenses for bonuses and rebates	-71,482	-57,635
of which performance-based	-70,242	-57,600
of which non-performance-based	-1,241	-35
Unrealized losses on investments	-7,278	-1,338
Insurance business operating expenses	-277,898	-283,908
of which front-end fees	-116,521	-118,231
of which administrative expenses	-163,586	-165,958
of which reinsurers' share	2,209	281
Investment expenses allocated to the underwriting account	-32,542	-47,778
Miscellaneous underwriting expenses for own account	-25,489	-27,537
<b>Total underwriting expenses</b>	<b>-1,355,441</b>	<b>-1,319,472</b>
<b>Subtotal</b>	<b>10,811</b>	<b>13,749</b>
Change in the equalization provision and similar provisions	-7,585	-4,425
<b>Underwriting result for own account</b>	<b>3,225</b>	<b>9,325</b>
Income from investments	323,308	329,744
Expenses for investments	-50,578	-74,684
<b>Gains and losses on investments</b>	<b>272,730</b>	<b>255,060</b>
Gains and losses on investments assigned to the underwriting account	-178,991	-160,246
Revenue of non-insurance companies	98,002	108,492
Cost of goods and services provided by non-insurance companies to generate revenue	-92,719	-103,890
<b>Gross profit</b>	<b>5,283</b>	<b>4,602</b>
Other income	27,040	21,270
Other expenses	-64,326	-71,927
<b>Other net income/expense</b>	<b>-37,286</b>	<b>-50,658</b>
<b>Profit/loss from ordinary activities</b>	<b>64,961</b>	<b>58,083</b>
<b>Net extraordinary income/expense</b>	<b>-267</b>	<b>-267</b>
<b>Profit/loss before tax</b>	<b>64,695</b>	<b>57,816</b>
Tax expense		
<b>Net income for the year</b>	<b>64,695</b>	<b>57,816</b>
of which non-controlling interests		

International		Total		Consolidation		Group total	
2016	2015	2016	2015	2016	2015	2016	2015
<b>603,003</b>	<b>560,590</b>	<b>1,729,698</b>	<b>1,656,058</b>	<b>0</b>	<b>0</b>	<b>1,729,698</b>	<b>1,656,058</b>
427,314	404,051	1,531,645	1,477,728	0	0	1,531,645	1,477,728
175,689	156,539	198,054	178,330	0	0	198,054	178,330
-4,258	-3,628	-18,881	-16,143	0	0	-18,881	-16,143
1,899	-4,041	-4,371	-8,680	0	0	-4,371	-8,680
<b>600,644</b>	<b>552,921</b>	<b>1,706,447</b>	<b>1,631,235</b>	<b>0</b>	<b>0</b>	<b>1,706,447</b>	<b>1,631,235</b>
0	0	37,395	27,650			37,395	27,650
0	313	212,166	208,951	-2,322	-2,247	209,844	206,704
0	0	1,605	9,373	0	0	1,605	9,373
172	157	9,454	9,405	0	0	9,454	9,405
<b>600,816</b>	<b>553,392</b>	<b>1,967,067</b>	<b>1,886,614</b>	<b>-2,322</b>	<b>-2,247</b>	<b>1,964,745</b>	<b>1,884,367</b>
-260,739	-245,935	-1,014,879	-974,611	0	0	-1,014,879	-974,611
26	-218	-186,586	-172,818	0	0	-186,586	-172,818
0	0	-71,482	-57,635	0	0	-71,482	-57,635
0	0	-70,242	-57,600	0	0	-70,242	-57,600
0	0	-1,241	-35	0	0	-1,241	-35
0	0	-7,278	-1,338	0	0	-7,278	-1,338
-268,576	-246,838	-546,474	-530,746	0	0	-546,474	-530,746
-56,125	-50,710	-172,646	-168,941	0	0	-172,646	-168,941
-214,851	-197,627	-378,437	-363,585	0	0	-378,437	-363,585
2,400	1,499	4,609	1,780	0	0	4,609	1,780
0	0	-32,542	-47,778	0	0	-32,542	-47,778
-488	-11	-25,978	-27,548	0	0	-25,978	-27,548
<b>-529,778</b>	<b>-493,002</b>	<b>-1,885,218</b>	<b>-1,812,474</b>	<b>0</b>	<b>0</b>	<b>-1,885,218</b>	<b>-1,812,474</b>
<b>71,038</b>	<b>60,390</b>	<b>81,849</b>	<b>74,140</b>	<b>-2,322</b>	<b>-2,247</b>	<b>79,527</b>	<b>71,893</b>
-5,206	-1,358	-12,792	-5,783	0	0	-12,792	-5,783
<b>65,832</b>	<b>59,032</b>	<b>69,057</b>	<b>68,357</b>	<b>-2,322</b>	<b>-2,247</b>	<b>66,735</b>	<b>66,110</b>
27,410	27,100	350,718	356,844	-56,644	-64,432	294,075	292,412
-7,671	-7,060	-58,249	-81,743	4,196	374	-54,053	-81,370
<b>19,739</b>	<b>20,041</b>	<b>292,470</b>	<b>275,101</b>	<b>-52,448</b>	<b>-64,059</b>	<b>240,022</b>	<b>211,042</b>
0	0	-178,991	-160,246	2,322	2,247	-176,669	-157,999
0	0	98,002	108,492	-43,173	-41,852	54,830	66,640
0	0	-92,719	-103,890	43,173	41,852	-49,547	-62,038
<b>0</b>	<b>0</b>	<b>5,283</b>	<b>4,602</b>	<b>0</b>	<b>0</b>	<b>5,283</b>	<b>4,602</b>
2,214	2,554	29,254	23,823	0	657	29,254	24,480
-10,143	-6,453	-74,469	-78,380	-3,117	-3,120	-77,586	-81,501
<b>-7,929</b>	<b>-3,899</b>	<b>-45,215</b>	<b>-54,557</b>	<b>-3,117</b>	<b>-2,464</b>	<b>-48,332</b>	<b>-57,021</b>
<b>77,642</b>	<b>75,173</b>	<b>142,603</b>	<b>133,257</b>	<b>-55,564</b>	<b>-66,522</b>	<b>87,039</b>	<b>66,734</b>
<b>0</b>	<b>0</b>	<b>-267</b>	<b>-267</b>	<b>0</b>	<b>0</b>	<b>-267</b>	<b>-267</b>
<b>77,642</b>	<b>75,173</b>	<b>142,337</b>	<b>132,990</b>	<b>-55,564</b>	<b>-66,522</b>	<b>86,772</b>	<b>66,467</b>
				-43,654	-37,240	-43,654	-37,240
<b>77,642</b>	<b>75,173</b>	<b>142,337</b>	<b>132,990</b>	<b>-99,219</b>	<b>-103,763</b>	<b>43,118</b>	<b>29,227</b>
				314	-34	-314	-34

## Auditor's Report\*

We have audited the consolidated financial statements, comprising the balance sheet, income statement, notes to the financial statements, cash flow statement, statement of changes in equity, and segment reporting, together with the group management report prepared by ARAG Holding SE, Düsseldorf, for the financial year from January 1, 2016 to December 31, 2016. The preparation of the consolidated financial statements and the group management report in accordance with the requirements of German commercial law is the responsibility of the Company's Management Board. Our responsibility is to express an opinion on the consolidated financial statements and the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with section 317 of the German Commercial Code (HGB) and German generally accepted auditing standards promulgated by the Institute of Public Auditors in Germany (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with German accepted accounting principles and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the financial statements of the entities included in the consolidated financial statements, the determination of the entities to be included in the consolidated financial statements, the accounting and consolidation principles used and significant estimates made by the Management Board, as well as evaluating the overall presentation of the consolidated financial statements and the group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

\* Voluntary translation. It should be noted that only the German Auditor's Report, which is based on the audit of the German version of the Company's consolidated financial statements, is authoritative.

In our opinion, based on the findings of our audit, the consolidated financial statements comply with the legal requirements and give a true and fair view of the net assets, financial position, and results of operations of the Group in accordance with German accepted accounting principles. The group management report is consistent with the consolidated financial statements, complies with the legal requirements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Düsseldorf, April 13, 2017

PricewaterhouseCoopers GmbH  
Wirtschaftsprüfungsgesellschaft

Ludger Koslowski  
Wirtschaftsprüfer (German Public Auditor)

Sven Capousek  
Wirtschaftsprüfer (German Public Auditor)

## Report of the Supervisory Board

The Supervisory Board continually monitored and advised the Management Board during the financial year, holding five ordinary Supervisory Board meetings for this purpose. There was also one extraordinary meeting of the Supervisory Board, and two resolutions were adopted in writing. Monitoring was based on the written and oral reports presented by the Management Board, who provided the Supervisory Board with timely and comprehensive information on relevant planning matters, the performance of the Company and its equity investments, the risk situation, and risk management. The Supervisory Board also received detailed information between meetings on projects and plans of particular importance or urgency to the Company. At the meetings, the Management Board agreed the Company's strategic direction with the Supervisory Board. The Supervisory Board was involved in decisions of fundamental importance to the Company. Progress on implementing the strategy was regularly discussed in the meetings.

The main topics deliberated on during the Supervisory Board meetings included the influence of the phase of low interest rates and the strategy to deal with the investee company ARAG Lebensversicherungs-AG, the business performance of the investee company ARAG SE, the business performance of the branches and Group companies outside Germany, and the investment in the Group's own real estate, including reporting on the occupancy rate.

In the process of selling the investee company ARAG Lebensversicherungs-AG, the Supervisory Board adopted the resolutions proposed by the Management Board on the implementation of the sale.

The Supervisory Board also regularly received explanations regarding risk reporting from the Management Board and discussed the risk strategy and the corporate strategy.

Finally, the Supervisory Board examined the allocation of responsibilities among the members of the Management Board and the appropriateness of the Management Board's remuneration.

The Supervisory Board also studied the Company's risk strategy.

No special monitoring measures were required last year. The Supervisory Board believes that the Management Board manages the business lawfully, properly, and appropriately. In particular, the Management Board fulfills its duty of care regarding the Company's continued existence and long-term profitability.

The Supervisory Board reviewed the consolidated financial statements and group management report. To do so, it exercised its powers pursuant to section 111 (2) of the German Stock Corporation Act (AktG) including, but not limited to, inspecting the books and papers of the Group companies. The review was conducted on the basis of the regular written and oral reports from the Management Board about the business situation and all major transactions and on the basis of the commercial-law accounting regulations.

The scope of the review of the consolidated financial statements also covered the accounting options exercised by the Management Board. The findings of the review were as follows:

1. The Management Board's financial reporting complies with the legal requirements and the provisions in the Group parent company's articles of incorporation. The group management report is consistent with the consolidated financial statements.
2. The accounting policy decisions that were made on a discretionary basis were exercised for the benefit of the Group and took shareholders' interests into account to an appropriate degree.

On behalf of the Supervisory Board, PricewaterhouseCoopers GmbH, Wirtschaftsprüfungsgesellschaft, Düsseldorf, audited the consolidated financial statements for the year ended December 31, 2016, including the bookkeeping system and the group management report, and issued an unqualified opinion. The audit report was presented to the Supervisory Board on time. Having studied the report and on the basis of its own final review, the Supervisory Board agrees with the auditor's opinion. It has no comments to make about the audit report.

There are no objections to be raised on the basis of the concluding findings of the review of the consolidated financial statements, group management report, and audit report.

Düsseldorf, May 10, 2017

The chairman of the Supervisory Board

Gerd Peskes

## Governing Bodies of the Company

**Supervisory Board** The members of the **Supervisory Board** are:

**Gerd Peskes** Wirtschaftsprüfer (German Public Auditor),  
Essen  
Chairman

**Prof. Dr. Dr. h. c. Rolf Dubs** University professor,  
St. Gallen/Switzerland  
Deputy chairman

**Dr. Tobias Bürgers** Attorney,  
Munich

**Management Board** **Dr. Dr. h. c. Paul-Otto Faßbender** Chief Executive Officer  
of ARAG SE,  
Düsseldorf

**Dr. Karl-Heinz Strohe** Attorney,  
Cologne  
(until July 31, 2016)

**Dr. Sven Wolf** Jurist,  
Krefeld  
(since January 1, 2016)

## Information

ARAG provides you with a broad range of information in many publications and on the internet about the Group and its insurance products and services. And as legal insurance is a core competency of ARAG, it also offers selected tips and advice on legal matters. If you have any questions, require an insurance quote, or are simply looking for some basic information, please get in touch or visit our website.

You can obtain up-to-date **information about the Group** using the following contact details:

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You can find the latest **information about the Group and our products** on our website:

**[www.ARAG.com](http://www.ARAG.com)**

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