

ARAG SE

2017 Annual Report

SINGLE-ENTITY FINANCIAL STATEMENTS



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Overview

ARAG SE Key Figures

(€'000)	2017	Change	2016	2015
Sales revenue				
Gross premiums written	870,004	5.50%	824,616	766,127
Premiums earned for own account	868,041	6.61%	814,252	756,133
Expenses				
Claims incurred net of reinsurance	462,746	11.40%	415,393	400,070
Claims ratio (basis: premiums earned)	53.3%	2.3% pts.	51.0%	52.9%
Own account insurance business operating expenses	389,181	6.80%	364,385	344,781
Cost ratio (basis: premiums earned)	44.8%	0.0% pts.	44.8%	45.6%
Net income overview				
Underwriting result for own account	14,841	-51.14%	30,377	11,267
Gains and losses on investments	73,016	0.46%	72,679	71,620
Other net income/expense	-31,066	-11.31%	-35,028	-39,291
Profit/loss from ordinary activities	56,791	-16.52%	68,028	43,596
Net extraordinary income/expense	0	n.a.	0	0
Net income for the year	32,031	1.16%	31,663	22,963
Key ratios				
Technical provisions/ net premiums earned	151.7%	-4.8% pts.	156.5%	166.2%
Equity/premiums earned	50.6%	-1.3% pts.	51.9%	53.7%

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. Besides legal insurance, it offers its customers in Germany attractive, needs-based products and services covering casualty and property, health, and pension insurance. In the area of digitalization – one of the major challenges going forward – ARAG has been responding rapidly, using its professional expertise to continuously implement innovative, beneficial ideas, thereby delivering further value added for the customer. 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 Canada) through branches, subsidiaries, and equity investments. It generates sales revenue and premiums of more than €1.6 billion and employs around 4,000 people.

ARAG SE is responsible for strategic Group management and the legal insurance operating business at both domestic and international levels. The ARAG insurance and service companies are responsible for the other lines of business and the related operational management. 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 units outside Germany 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 a competitive provider of property, liability and accident insurance policies. 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 attractive brokering products 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 offers a broad range of highly efficient products, emphasizing its appeal as one of the best providers of full-coverage and supplementary health insurance. ARAG Core Sales also offers products from its strategic partner Alte Leipziger, perfectly complementing ARAG's range of services with a retirement pension offering.

Management Report of ARAG SE

I. Company Fundamentals

Business model

ARAG SE 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 product concepts aimed at both private and small business customers. The modular structure of these concepts means that insurance can be precisely tailored to the requirements of each customer.

An important role is also played by customized legal insurance products designed for particular target groups.

ARAG SE is the provider of legal insurance for private customers and small businesses. It does not operate diversified corporate insurance business. In the international markets, it also operates travel insurance business in connection with its provision of legal insurance.

ARAG began to operate outside Germany for the first time 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. Today, ARAG operates in a total of 17 countries (Germany, 14 other European countries, the US, and – since 2016 – Canada) through branches, subsidiaries, and equity investments.

In addition to the Group headquarters in Düsseldorf, ARAG SE maintains operational branches in Austria, Belgium, Greece, Italy, the Netherlands, Portugal, Slovenia, and Spain. This centralized, star-shaped organizational structure emerged from the merger of previously independent subsidiaries in 2012. The international branches run their operating businesses in their national markets independently, taking into account the specific local circumstances in each case.

ARAG SE is one of the most internationalized insurers in Germany with 59.9 percent of its total gross premiums written accounted for by international business.

Scope of operations

In Germany, ARAG SE's activities are limited to just one class of insurance: legal insurance. In Italy, Spain, and Portugal, it also operates legal-insurance-related special service package business in addition to legal insurance business.

The territory covered by ARAG SE includes Germany as well as the Netherlands, Belgium, Austria, Slovenia, Italy, Spain, Portugal, and Greece. ARAG SE's business outside Germany is operated by the branches.

Legal insurance is also provided in the US, Norway, Sweden, and – since 2015 – Denmark. In each case the business is operated through legally independent affiliated companies, which are all managed uniformly by ARAG SE as the 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 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, where ARAG has been offering legal insurance through a Group company since the end of 2016.

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

Sales organization

In 2017, the close integration between the Sales and the Products and Innovation units was taken a step further with the creation of a new Group area of responsibility to be referred to as 'Sales, Products and Innovation'. All sales channels are now operating as one and are already enabling ARAG to leverage valuable synergies.

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. From 2018, all applications for legal, property, liability, and accident insurance will no longer be printed out separately, reflecting in particular the key issues of sustainability in the ARAG Group and the steady advance of digitalization. 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. The broad-based and regularly updated range of courses in this training ensures the exclusive agents receive high-quality training and development covering ARAG and its products. The aim of the holistic advice is to clearly establish the customer's current situation and needs regarding insurance and then to develop precisely tailored solutions, taking into account all statutory requirements.

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. In the year under review, the online broker portal also continued to be revised and expanded.

In addition, ARAG increased its customer base in online business to more than 230,000 customers. This equates to almost 11 percent of the German customer base. ARAG's online business is therefore increasingly turning into a further strong sales channel. In Germany, the ARAG Group's sales channel mix also includes sales partnerships in which made-to-measure, high-performance ARAG insurance solutions are offered under partnership agreements with other insurance companies, banks, other companies, associations, and clubs.

Insurance portfolio

The breakdown of the insurance portfolio (number of policies) as of the end of the reporting year was as follows:

Insurance portfolio		
(No.)	Dec. 31, 2017	Dec. 31, 2016
German	1,495,840	1,446,227
International	2,664,666	2,692,257
Total	4,160,506	4,138,484

Types of insurance in the insurance business

The range of products offered by ARAG SE in Germany includes all the types of insurance in the legal insurance class of insurance listed in the General Terms and Conditions for Legal Insurance plus financial loss legal insurance for members of supervisory boards, advisory councils, and management boards, and for senior managers. Subject to special terms and conditions of insurance, ARAG SE offers legal insurance covering victims' proceedings, divorce, maintenance payments issues, and criminal proceedings; in collaboration with its subsidiary ARAG Allgemeine Versicherungs-AG, it also offers 'Recht&Heim Aktiv', a bundled product providing all-round cover. In addition, ARAG SE is increasingly operating inward reinsurance business with third parties.

In Spain and Italy, ARAG SE's range of legal insurance products is complemented by policies that mitigate the financial consequences if a policyholder loses his or her driver's license. The Company also operates travel insurance business in Spain and Portugal.

II. Report on Economic Position

Economic and sector conditions

In 2017, the recovery in the global economy gained significant momentum compared with the previous year. The pace of growth in global gross domestic product (GDP) picked up markedly. In particular, growth in the eurozone has recently been unexpectedly strong. The economic situation in many emerging markets has also improved, which can be attributed, at least in the case of oil-exporting countries, to stabilization of the price of crude oil. Together with the favorable financing terms available, the high levels of capacity utilization already reached in many businesses, and an expansionary economic policy, this has led to an increase in capital spending and an accompanying upturn in global trade. As a consequence of the economic recovery, the labor market has also improved markedly in many economies, notably in the US and Japan. Unemployment rates are now falling again significantly in many countries.

Risks previously threatening the recovery have not materialized or, at least, have diminished. Although the vote in favor of Brexit and the subsequent exit negotiations have indeed slowed growth in the United Kingdom, there has been no economic slump.

In the eurozone, the unexpectedly strong economic recovery has extended to all the member countries. Currently, consumer spending is the most significant driver behind the upturn, although some of the growth has also been attributable to the continuation in the very expansionary monetary policy. In addition, the structural adjustments in many of the member countries since the financial crisis are likely to have been significant factors contributing to the brighter economic conditions. Both capital investment and exports were up sharply, reflecting dynamic growth in both of these areas. Employment also went up again in the eurozone in 2017. The German Council of Economic Experts currently estimates that total eurozone production grew by 2.3 percent in 2017.

The German economy is benefiting from a long sustained period of robust growth, built on ever-broader foundations. This growth is being driven by strong domestic demand, economic recovery in the eurozone, and economic policy that remains expansionary. While government spending and investment in construction have been increasing steadily for some time, spending on capital equipment and research & development expenditure are now also rising more quickly again. In addition, growth in key sales markets, particularly in the eurozone, has recently been gathering pace significantly. In Germany, household consumption continues to be the single greatest factor fueling the economic growth. Consumer sentiment is very favorable, supported by a willingness to spend and positive income expectations. Consumer spending growth rates are being maintained at a very high level. This is closely associated with the ongoing improvement in the number of people in work and the sharp rise in real disposable incomes.

The German Council of Economic Experts has predicted a 2.0 percent rise in real GDP for 2017. Adjusted for the different number of working days, the rise is as much as 2.3 percent. This means that a German economic boom is gradually developing. A growth rate of 1.4 percent is forecast for 2018. Against this backdrop and the very slow normalization of monetary policy by the European Central Bank (ECB), but combined with steady energy prices, the increase in inflation in 2018 is likely to remain modest. Looking further ahead however, inflation is projected to rise over the medium term.

Following the fall in the capital market rate (yield on listed German government securities with a residual maturity of nine to ten years) in the summer of 2016 to a historic low of minus 0.2 percent, this rate rose again in the period up to July 2017 to just over 0.6 percent. Overall, however, the capital market rate has remained at a relatively low level. Share prices benefited from these favorable macroeconomic conditions. Whereas the EURO STOXX 50's increase of 6.5 percent was still notable, the performance of the German DAX share index was even more significant, climbing by 12.6 percent to 12,918 points at the end of the year.

The German Insurance Association (GDV) is projecting that premiums will have grown year on year in 2017. According to these forecasts, total gross premiums written in 2017 will have risen by approximately 1.3 percent compared with the previous year (2016: 0.2 percent).

Premium income in direct casualty and property insurance business is expected to have increased by 2.9 percent (2016: 2.9 percent). The reasons included increases in the sums insured and extension of the cover in property insurance. From the perspective of claims incurred, a number of rather minor storm events were the main features of 2017. For example, according to the GDV, storms at the end of the first half of the year caused insured losses of approximately €300 million. Nevertheless, the claims incurred equated to an increase compared with 2016, which had been a below-average year in terms of storm and hail events. Accordingly, based on GDV projections, underwriting losses are anticipated in the residential buildings insurance segment.

The legal insurance class of insurance also saw strong premium growth of around 4.0 percent, primarily as a result of opportunities to adjust premiums, although the increase was lower than in the previous year (2016: 5.7 percent). Opportunities to adjust premiums available as of October 1, 2017 will generate a further increase in premiums in the industry in 2018. Following three years of underwriting losses in this class of insurance, there will still be no underwriting profit for a fourth year, even though the growth in premiums exceeded the increase in claims incurred: According to a GDV forecast, the industry-wide combined ratio in 2017 was approximately 100 percent.

Based on premium adjustments, the private health insurance segment also anticipated significant premium growth of around 3.5 percent in 2017 (2016: 1.2 percent). In the beneficial economic conditions, the rising number of employment contracts subject to social security contributions had a positive impact on the portfolio of comprehensive insurance contracts.

Business performance

The sustained favorable economic trends in Germany and Europe were also reflected in the business performance of ARAG SE. Gross premiums written rose by a further 5.5 percent year on year from €824,616.0 thousand to €870,004.1 thousand. The increase in premiums arose from business growth in all units – both in Germany and abroad. In the international markets, the increases were mainly generated from indirect business. In the challenging Italian and Spanish markets, dynamic growth was sustained, generating clear premium gains. The branch in Austria also performed well overall following a comprehensive restructuring phase. ARAG SE was able to achieve further expansion in its business in its largest international market, the Netherlands. A clear increase in business volume was also generated in the strictly divided legal insurance market in Belgium. The portfolio in Germany expanded not only because of premium adjustments and low lapse rates, but primarily because of the success in gaining new business from Partner Sales and online sales.

Of the total premium income, €673,251.8 thousand (2016: €633,818.0 thousand) was derived from direct business. At the international branches, travel insurance business and financial loss insurance business with a value of €58,373.0 thousand (2016: €50,720.2 thousand) was generated in connection with legal insurance business. Direct legal insurance business accounted for €614,878.8 thousand (2016: €583,097.8 thousand). Gross premiums written in the direct legal insurance business in Germany increased by 6.1 percent, from €329,272.1 thousand to €349,202.4 thousand. This steady growth in premiums since 2013 is attributable to a high level of new business combined with a constantly low level of lapses. After deduction of the reinsurers' shares and changes in unearned premiums, the remaining net premiums earned for all business amounted to €868,014.4 thousand compared with €814,252.3 thousand in 2016.

With the overall increase in business volume, claim payments dropped to 48.6 percent of premiums earned (2016: 50.2 percent). Claims incurred amounted to €462,745.8 thousand compared with €415,393.0 thousand in 2016. Despite comprehensive claims settlement optimization, the claims ratio rose from 51.0 percent in 2016 to 53.3 percent in the year under review. One of the factors that contributed to this increase was the higher level of claims incurred in legal insurance in connection with the diesel emissions issue.

Insurance business operating expenses also increased. The cost ratio remained steady at 44.8 percent – despite the sharp rise in pension and other post-employment benefit expenses, the higher commissions in connection with the increase in new business, and the greater level of expenses for salaries and social security contributions resulting from growth in the number of employees. No year-on-year change in operating expenses clearly had a beneficial impact on the ratio in the year under review.

After taking into account the sundry underwriting income and expenses (net income of €1,804.4 thousand), the underwriting result for own account before the equalization provision declined to a profit of €17,919.5 thousand compared with a profit of €35,933.0 thousand in 2016. A total of €3,078.8 thousand was added to the equalization provision in respect of the travel insurance business in Spain and Italy and the inward legal reinsurance business in a number of countries.

After the addition to the equalization provision, the underwriting result amounted to a profit of €14,840.7 thousand (2016: €30,376.6 thousand). Investments generated a net gain of €73,015.9 thousand (2016: €72,678.6 thousand). Despite the persistently low interest rates, ordinary income from securities went up from €33,791.9 thousand to €35,004.8 thousand. In 2016, significant reversals of write-downs had been recognized as a result of the fall in interest rates (€8,939.3 thousand), but in the year under review such reversals were much lower at €4,086.7 thousand. Transfers of profit from subsidiaries under profit-and-loss transfer agreements were €3,945.2 thousand higher than in 2016.

With regard to other net income/expense, the net expense decreased from €35,027.7 thousand in 2016 to €31,065.9 thousand in the reporting year. Improved net interest income/expense on tax refunds and retrospective tax payments as well as gains on the euro/pound sterling exchange rate contributed to this change.

At €56,790.6 thousand, profit before tax therefore remained at a sound level, although lower than the very high prior-year figure of €68,027.5 thousand.

After deduction of the tax expense of €24,759.5 thousand (2016: €36,365.0 thousand), net income for the year amounted to €32,031.2 thousand compared with €31,662.5 thousand in 2016. The tax expense for the previous year included €24,671.4 thousand resulting from write-downs on deferred tax assets. In the year under review, an amount of €6,080.4 thousand was derecognized from net deferred tax assets relating to the international branches.

Financial performance by source country

Performance in Germany

Direct insurance business Gross premiums written in direct business grew by 6.1 percent year on year. Gross premiums amounted to €349,202.4 thousand compared with €329,272.1 thousand in 2016. After deduction of reinsurance premiums and the change in unearned premiums, net premiums earned came to €345,275.3 thousand (2016: €324,555.4 thousand).

As a result of the growth in the insurance portfolio, claim payments rose by 0.6 percent, from €194,091.0 thousand in 2016 to €195,206.0 thousand in the year under review. Claims incurred rose by 9.0 percent to €225,186.1 thousand in the reporting year. The increase in the number of claims reports from 335,605 in 2016 to 338,196 in 2017 only had a small impact on claims incurred. Despite the growth in the portfolio, the claims ratio for

2017 (gross) at 65.2 percent was higher than the equivalent 2016 figure of 63.6 percent. A total of 432,252 claims (2016: 427,276 claims) were reported in the year under review, a year-on-year rise of 1.2 percent.

Reinsurers' shares amounting to €1,017.3 thousand (2016: €170.0 thousand) were recognized as income in 2017. The remaining recognized claims incurred came to €220,646.6 thousand as against €196,962.5 thousand in 2016. The claims ratio (net) based on the recognized claims incurred was 63.9 percent compared with 60.7 percent in 2016.

Gross insurance business operating expenses rose from €140,182.8 thousand in 2016 to €152,290.3 thousand in the reporting year. Commissions went up by 5.6 percent in 2017 from €77,856.4 thousand to €82,189.7 thousand in line with the increase in premiums. Other primary administrative expenses (before cost allocations) went up in the year under review from €158,809.6 thousand to €176,630.7 thousand. As well as a rise of €4,673.6 thousand in wages and salaries due to new hires and collectively agreed pay rises, an increase of €12,667.6 thousand in pension and other post-employment benefit expenses contributed significantly to this increase. In 2016, a change to the statutory discount rate, which had been implemented by the government in view of the persistently low interest rates, had led to a one-off fall in pension and other post-employment benefit expenses. As a result of these changes, the cost ratio rose from 43.2 percent in 2016 to 44.1 percent in the year under review.

As a consequence of the greater business volume combined with the rise in costs and higher claims ratio, the underwriting result before the equalization provision in the direct insurance business deteriorated from a loss of €11,329.3 thousand in 2016 to a loss of €26,159.7 thousand in the reporting year.

There was no requirement to recognize an equalization provision pursuant to section 29 of the German Regulation on the Accounting of Insurance Undertakings (RechVersV) for the direct business owing to the low level of volatility.

Inward reinsurance business In Germany, the Company takes on inward reinsurance business from primary insurers of third-party business in the United Kingdom under quota-share reinsurance treaties. The business with one of these insurers is being run off. There are also reinsurance treaties with a subsidiary in the US (excess of loss treaty) and with a primary insurer in Canada (quota-share treaty). Net premiums amounted to €21,922.2 thousand compared with €22,491.4 thousand in 2016. The fall in the nominal business volume was attributable to changes in the euro/pound sterling exchange rate. After taking into account claims incurred of €20,037.9 thousand (2016: €15,638.3 thousand) and administrative expenses of €1,032.3 thousand (2016: €1,087.3 thousand), this led to an underwriting profit before the equalization provision of €852.0 thousand (2016: €5,765.7 thousand).

A sum of €232.1 thousand was added to the equalization provision (2016: €350.0 thousand). The underwriting result for the inward reinsurance business amounted to a profit of €619.9 thousand (2016: €5,415.7 thousand).

Non-underwriting result

The ECB again maintained its expansionary monetary policy with only hesitant adjustments. Accordingly, interest rates persisted at a low level without any prospect of change in the immediate future. In turn, this led to ever-decreasing investment income. In the year under review, it was therefore only possible to generate ordinary income from investments of €20,289.5 thousand, whereas the equivalent figure in 2016 had been €21,092.9 thousand. As interest rates were no longer falling any further and the potential for reversing write-downs was becoming increasingly exhausted, there was also contraction in reversals of write-downs and in gains on disposal. Reversals of write-downs were mainly applied in respect of investment fund shares/units in an amount of €3,638.6 thousand (2016: €5,074.8 thousand). On the other hand, write-downs were applied in respect of securities in an amount of €1,929.2 thousand (2016: €911.1 thousand). Current income of €2,374.5 thousand was generated from land. This represented a decline compared with the prior-year figure of €2,791.8 thousand owing to tax adjustments in connection with indirectly held real estate. Dividend income from affiliated companies and equity investments rose by €6,323.6 thousand year on year. Equity investments in the US, UK, and Switzerland maintained their very sound financial performance. The profit transferred from ARAG Allgemeine Versicherungs-AG went up to €17,964.4 thousand, which was significantly higher than the prior-year figure of €14,019.2 thousand.

Write-downs of shares in affiliated companies had only been necessary in 2016 in an amount of €1,512.6 thousand. The disposal of fixed-income securities only gave rise to a very low level of losses on the disposals. The realized gains on disposal of €1,121.8 thousand in the year under review arose from the sale of institutional fund shares/units. The gains on disposal realized in 2016 amounting to €3,708.1 thousand were generated by an additional pro-rata sale of indirectly held real estate. Net gains on investments came to €58,233.3 thousand in the year under review compared with €55,820.0 thousand in 2016. Ordinary gains and losses on investments – after deduction of the expenses for the management of the investments – amounted to a net gain of €55,532.6 thousand (2016: €47,325.1 thousand) and led to a current average yield of 4.9 percent (2016: 3.5 percent).

Other net income/expense amounted to a net expense of €27,716.4 thousand (2016: €27,616.3 thousand). The other net income/expense figure includes the offset income and expense from the provision of services to Group companies and expenses to which income cannot be directly assigned. The latter expenses include addition of interest to the pension provision, Supervisory Board and Advisory Council remuneration, year-end costs, general legal and tax consultancy expenses, costs incurred in relation to the Solvency II regulatory regime, and the interest expense on subordinated liabilities. In the year under review, an improvement in the brokerage business and the positive impact of changes in the euro/pound sterling exchange rate more than made up for the one-off reduction in the net expense that occurred in 2016 (switch in the discounting of defined benefit obligations for people who have already retired).

Net extraordinary income/expense

No extraordinary income or expense was recognized in either 2017 or 2016.

Taxes

Income taxes also include the impact on net income from deferred taxes in accordance with section 274 of the German Commercial Code (HGB). In 2016, the change in deferred taxes had led to a reduction in the net income for the year of €24,671.4 thousand, as it was expected that there would be no impact on current taxes at the projected time of reversal. Net deferred tax assets were no longer recognized on the balance sheet in the year under review. Current taxes amounted to income of €1,320.2 thousand (2016: income of €831.8 thousand) and were attributable in full to prior years. The total amount of miscellaneous taxes included a non-recurring amount related to the findings of a tax audit outside Germany. Taking into account the miscellaneous taxes, the total tax expense came to €682.2 thousand compared with €24,759.3 thousand in 2016.

Net income/loss for the year, Germany

The net income for the year generated by the German business of ARAG SE amounted to €4,295.0 thousand (2016: net loss of €2,469.2 thousand).

Branch performance

The eight European branches of ARAG SE enjoyed significant further growth overall, with gross premium income advancing by 5.5 percent to €498,879.6 thousand (2016: €472,852.5 thousand). The branches accounting for the highest level of premiums written were ARAG Netherlands with premiums written of €142,459.8 thousand (2016: €140,141.0 thousand), ARAG Spain with €139,039.7 thousand (2016: €124,505.6 thousand), and ARAG Italy with €123,519.2 thousand (2016: €118,417.6 thousand). The premiums earned for own account amounted to a total of €500,843.9 thousand (2016: €467,205.5 thousand). The growth was generated from new contracts in indirect business, the ongoing systematic development of insurance products in legal-insurance-related business, and further expansion of sales channels.

Claims incurred of €222,061.3 thousand (2016: €202,792.2 thousand) and insurance business operating expenses of €235,857.9 thousand (2016: €223,114.6 thousand) reflect a generally steady level of performance with a slightly increased claims ratio of 44.3 percent (2016: 43.4 percent). Higher commission expenses were offset by the growth-related fixed-cost depression, as a result of which the cost ratio was calculated at 47.1 percent for the year under review, which was actually slightly lower than the corresponding figure for the previous year (47.8 percent). Including miscellaneous underwriting income and expenses of €302.5 thousand, the underwriting result before the equalization provision generated by the international legal insurance business amounted to a slightly improved profit year on year of €43,227.2 thousand (2016: €41,496.5 thousand). After an addition to the equalization provision of €2,846.7 thousand (2016: €5,206.4 thousand), a profit of €40,380.5 thousand was reported under the underwriting account (2016: €36,290.2 thousand).

The investments assigned to the branches generated a total net gain on investments of €14,782.5 thousand (2016: €16,858.6 thousand). A notable year-on-year change in this regard was that the income from reversals of write-downs and from disposals fell to €802.3 thousand in the year under review (2016: €6,805.8 thousand). On the other hand, ordinary gains on investments rose to €18,065.0 thousand (2016: €15,104.3 thousand) on the back of higher dividends from institutional funds.

Other net income/expense amounted to an expense of €3,349.5 thousand (2016: expense of €7,411.4 thousand). The 2016 figure had included additional charges related to structural changes and amortization of goodwill in Spain as well as expenses arising in connection with the expansion of the online business in the Netherlands.

The branches generated profit from ordinary activities of €51,813.5 thousand (2016: €45,737.4 thousand). Including deferred taxes, the tax expense came to €24,077.3 thousand (2016: €11,605.7 thousand). In the year under review, this included an expense of €6,080.4 thousand from the derecognition of net deferred tax assets.

With net income for the year of €27,736.2 thousand in 2017 (2016: €34,131.8 thousand), the European branches are continuing to make a very high contribution to the overall net income of ARAG SE over the long term.

Overall net income for the year

The financial performance of ARAG SE over the reporting year was characterized by the growth in business activities across its entire operations and by the impact of low interest rates on capital markets. Commission increases resulting from the higher level of new business and from new inward reinsurance treaties also contributed to cost increases, as did additional staff costs arising from the increasing administrative duties in the central functions of the Group, which are carried out by ARAG SE as the Operating Group Holding Company. The steady expansion of business at the international branches added to the costs. Furthermore, costs in 2016 had been reduced by the significant positive impact of a non-recurring item. This item was the statutory change relating to the determination of the discount rate used to discount defined benefit obligations. The trend in claims led to a claims rate of 53.3 percent compared with 51.0 percent in 2016. Underwriting profit before the equalization provision amounted to €17,919.5 thousand, which, despite being a significant positive figure, was nevertheless lower than the prior-year figure of €35,933.0 thousand. After the addition to the equalization provision, which was required in particular for the inward reinsurance business segments, the remaining underwriting profit amounted to €14,840.7 thousand (2016: €30,376.6 thousand).

The net gains on investments (after deducting the corresponding expenses) came to €73,015.9 thousand (2016: €72,678.6 thousand). The ECB's monetary policy did not permit any notable increases in interest rates in the year under review. Higher income from institutional funds offset the fall in interest income from fixed-income investments. However, there was no further fall in interest rates, with the result that further reversals of write-downs on securities were no longer recognized to any great extent. Ordinary gains on investments rose sharply year on year to €73,597.6 thousand (2016: €62,429.4 thousand) as a consequence of greater profit transfers from subsidiaries. By contrast, gains on disposal and reversals of write-downs were substantially lower.

Other net income/expense improved again year on year, the main factors being the improvement in the brokerage business and the impact of changes in the euro/pound sterling exchange rate. Profit before tax amounted to a total of €56,790.6 thousand. In line with forecasts, this was below the prior-year figure of €68,027.5 thousand.

After deduction of the tax expense, net income for the year amounted to €32,031.2 thousand (2016: €31,662.5 thousand). In 2016, the tax expense had included an additional expense of €24,671.4 thousand arising from the revaluation of net deferred tax assets. An equivalent expense of €6,080.4 thousand arose in the reporting year. After taking into account the profit brought forward from 2016, the net retained profit to be presented to the Annual General Meeting for a decision on appropriation is €32,032.2 thousand (2016: €31,701.0 thousand).

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 €30,000.0 thousand that matures on July 29, 2024.

The underwriting liabilities are covered by investments of €1,911,846.5 thousand (December 31, 2016: €1,805,090.6 thousand). In addition to current bank balances and cash on hand of €116,272.4 thousand (December 31, 2016: €166,483.7 thousand), the Company has investments at its disposal that can be sold on the capital and financial markets at short notice, thus ensuring that the Company is able to satisfy its payment obligations under insurance contracts at all times.

Further information on the extent of spending on property and equipment, 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 18.

Cash flow statement*

(€)	2017	2016
Cash flows from operating activities		
Profit for the period	32,031,163	31,662,538
Increase(+)/decrease(-) in technical provisions, net	42,084,430	17,696,276
Increase(-)/decrease(+) in deposits with ceding insurers and in receivables from reinsurance business	-7,191,906	-10,189,058
Increase(+)/decrease(-) in deposits from reinsurers and liabilities from reinsurance business	205,650	-303,228
Increase(-)/decrease(+) in receivables from direct insurance business	387,093	-2,526,034
Increase(+)/decrease(-) in liabilities from direct insurance business	-1,570,138	1,938,400
Increase(-)/decrease(+) in miscellaneous receivables	2,394,451	6,832,836
Increase(+)/decrease(-) in miscellaneous liabilities	389,838	4,908,701
Change in miscellaneous balance sheet items not related to investing or financing activities	-87,660,967	-96,252,619
Other non-cash income and expenses, and adjustment of the profit/loss for the period	9,317,443	5,095,278
Gain(-)/loss (+) on the disposal of investments, property and equipment, and intangible fixed assets	-967,689	-8,546,203
Expenses for/income from extraordinary items	0	0
Income tax expense/income	22,181,607	35,156,509
Cash receipts from extraordinary items	0	0
Cash payments for extraordinary items	0	0
Income taxes paid	-84,238	17,551,628
Cash flows from operating activities	11,516,737	3,025,023
Cash flows from investing activities		
Proceeds from disposal of property and equipment	145,018	33,608
Proceeds from disposal of intangible fixed assets	14,030	45,807
Payments to acquire property and equipment	-3,147,828	-2,515,568
Payments to acquire intangible fixed assets	-3,137,319	-2,693,879
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
Cash flows from investing activities	-6,126,100	-5,130,031
Cash flows from financing activities		
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	-15,000,000	-15,000,000
Proceeds(+)/cash payments(-) related to miscellaneous financing activities	0	0
Cash flows from financing activities	-15,000,000	-15,000,000
Net change in cash and cash equivalents	-9,609,363	-17,105,008
Effect on cash and cash equivalents of exchange rate movements and remeasurements		
Cash and cash equivalents at beginning of period	67,912,842	85,017,850
Cash and cash equivalents at end of period	58,303,479	67,912,842

* The cash flow statement has been prepared in accordance with German accounting standard GAS 21 appendix 3.

Net assets

Investments The breakdown of investments, which increased by €106,755.9 thousand or 5.9 percent to €1,911,846.5 thousand as of December 31, 2017, was as follows:

Investments breakdown

(€'000)	Dec. 31, 2017		Dec. 31, 2016	
Land and buildings	93,557.6	4.9%	97,563.7	5.4%
Affiliated companies and equity investments	289,904.3	15.2%	241,905.3	13.4%
Lending to affiliated companies	0.0	0.0%	1,655.5	0.1%
Equities and investment fund shares/units	617,622.8	32.3%	625,493.3	34.7%
Bearer bonds	396,850.2	20.8%	301,550.4	16.7%
Loans secured by mortgages or land charges and fixed-income receivables	9,179.9	0.5%	3,975.0	0.2%
Registered bonds	140,511.3	7.3%	140,511.3	7.8%
Promissory notes, loans	251,959.9	13.2%	243,995.1	13.5%
Sundry lending	79.1	0.0%	150.1	0.0%
Bank deposits	57,969.0	3.0%	98,570.8	5.5%
Other investments	4,535.5	0.2%	5,331.3	0.3%
Deposits with ceding insurers	49,676.9	2.6%	44,388.8	2.4%
Total	1,911,846.5	100.0%	1,805,090.6	100.0%

Pursuant to section 341b HGB, equities and investment fund shares/units with a carrying amount of €599,848.9 thousand had been classified as fixed assets as of the balance sheet date (December 31, 2016: €605,838.0 thousand). Bearer bonds with a carrying amount of €9,980.0 thousand (December 31, 2016: €9,980.0 thousand) were treated as fixed assets.

The fair value of investments as of December 31, 2017 amounted to a total of €2,308,781.5 thousand compared with €2,271,678.3 thousand as of December 31, 2016. After taking into account the premium and discount amounts recognized under prepaid expenses and accrued income and under deferred income and accrued expenses in connection with the securities recognized at their nominal amount in accordance with section 341c HGB, the valuation reserves therefore amounted to €396,920.3 thousand as of the balance sheet date (December 31, 2016: €465,847.1 thousand).

Further information on the structure and changes in investments can be found in the overview under the non-insurance disclosures in the Notes.

Non-financial performance indicators

The ARAG Group has set out its self-image 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. Auf ins Leben.' (ARAG. Dive into life.) ARAG again added a wide range of new content to the section with the same title on its website www.ARAG.de in 2017. At the same time, it launched a new eye-catching brand marketing campaign at the end of April 2017. The underlying message, which is highly memorable, is that ARAG stands ready as a reliable partner with suitable solutions for anyone – young or old – who is open to something new. The centerpiece of the campaign was the 'Bereit' ['Ready'] commercial, which ran in movie theaters throughout Germany and also on various online channels. All the action in the clip centered on new plans and challenges, such as learning to drive, becoming a parent, or building a home. The ARAG commercial was supported by a number of other approaches, notably various social media activities. The content of the campaign launched in the first half of 2018 moves away from straightforward brand statements. It is now focusing on innovative new legal insurance products with retroactive cover and the huge significance of these products in terms of providing support for customers and consumers in their day-to-day lives.

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 ARAG believes it is critical to take the lead and shape the market with innovative, trend-setting product and service ideas. This approach is reflected in a wide variety of activities – most notably in the targeted expansion of the portfolio, which is constantly refined in the interests, and for the benefit, of customers.

This innovative strength is regularly confirmed by third parties: ARAG received a number of accolades in the Plus X Awards for innovation in the year under review. In the Innovation and Transparency categories, ARAG's Sofort legal insurance for motorists was singled out for an award, while ARAG received the Most Innovative Brand Award 2017 in the Insurance Companies category, an accolade that it had also received in the previous year.

ARAG has shown itself to be a trailblazer in the industry, based on exceptional product ideas. An excellent example is ARAG's Sofort legal insurance for motorists, introduced in 2016. This insurance offers retroactive cover and is unique in the German legal insurance market. Following this successful pilot project, a further policy with retroactive cover was designed in 2017 and launched at the beginning of February 2018: ARAG Sofort legal insurance for tenants provides retroactive cover for customers going back up to twelve months without any qualifying period. The legal insurance policy is available to individuals to cover losses in a total of five tenancy-related scenarios (e.g. legal problems in connection with rent increases, ancillary costs disputes, or, in the case of the 'Extra' variant, landlord's termination of a lease citing property required for his/her own use).

Complementing these product innovations, virtually all of ARAG's international branches and companies have adapted digital services such as live chat for policyholders and the ARAG Wallet-Card – which are already well established in the German market – and have successfully incorporated them as fixed components of their range of services.

In 2017, the ARAG Group launched the first advisory chatbot for insurance products on the German market, accompanied by a great deal of publicity. On Facebook Messenger, users can find out how best to minimize travel risks and can immediately take out the most suitable level of insurance cover online. The signal effect from this innovative service was not confined to Germany: ARAG SE's branch in Spain quickly adapted the chatbot and made it available on Facebook.

The ARAG Group is also constantly adding new pages to its websites – for both German and international users. For example, the relaunch of all German ARAG websites was successfully completed in the year under review. The model from both design and technical perspectives was, and continues to be, the continuously upgraded website at www.ARAG.de. In December 2017, this site was for the first time ranked as the best website out of a total of 126 insurance companies included in a regular survey carried out by AMC Finanzmarkt GmbH. ARAG achieved the outstanding overall score of 100 percent in this comparison of 'Insurance on the internet'.

The groupwide transfer of knowledge and technology has proven itself to be invaluable as a successful model when designing international ARAG websites. Further websites have been optimized in this way and standardized in terms of branding. In the year under review, ARAG Belgium, ARAG Austria, and ARAG Slovenia adopted the core Group solution when relaunching their websites. As a result, the Group is also presenting itself to best effect at an international level. In the first half of 2017, the ARAG Spain website for the first time came out top in the overall evaluation as part of a comparison run by Spanish insurance portal Innovación Aseguradora, in which 66 companies were assessed. The branch was also able to maintain this top ranking in the second half of the year.

The sales partners of ARAG Core Sales in Germany are also benefiting from the strong, completely revised websites with simple navigation and clear product structures. One of the features of the sites is that the sales partners can include their own, customized content. In addition, all new business concluded online using the website is assigned immediately to the relevant portfolio. In a further digital innovation, ARAG has introduced its own Facebook pages for the branch offices and for ARAG partners.

If the process of digitalization is to be successfully advanced in the widest possible range of activities, one of the fundamental requirements is that IT systems must be upgraded. In mid-2017, the Group reached a key milestone and bade farewell to the world of mainframe computers. Since then, ARAG has been operating with state-of-the-art Linux-based servers. This high-performance system architecture with distributed server systems meets future IT operating requirements, not least in terms of security and stability. ARAG has therefore already introduced systems that many competitors are still only starting to address. Another major project initiated in the year under review was the introduction of Office 365 software. The cloud-based office application will create new, flexible forms of collaboration and communication, both for ARAG employees and for sales part-

ners. Data protection, data security, and quality standards will be given top priority. Following the successful pilot phase in 2017, a rollout is scheduled to be completed at European level by the end of 2018.

Digitalization is a key theme in the Group and extends beyond digital services and IT system upgrades. ARAG is also actively exploiting the changes and opportunities associated with digitalization at a strategic level. It has created a separate new legaltech unit to position itself in the fiercely competitive legal advice market in Europe. To this end, in February 2017, it established Justix GmbH in Cologne as a wholly owned subsidiary of ARAG. Back in June 2017, the start-up launched its first business model, an online legal services platform under the brand name HelloLaw, in the Netherlands. The business is not restricted to existing customers.

Products As an innovative provider of high-quality insurance, the ARAG Group did more than simply launch brand new and innovative product concepts and services in Germany and its international markets in the year under review, it also constantly consolidated its existing product portfolio.

For example, in early 2017, it added an attractive variant to ARAG Recht&Heim, the Group's successful bundled product providing all-round cover for private customers encompassing legal, liability, and home contents insurance in one policy with an option for residential buildings cover. Previously, Recht&Heim was based on premium cover in each class of insurance. Now, ARAG has launched Recht&Heim Komfort for more price-sensitive customers – with comprehensive protection provided by the convenience-level cover for relevant areas of life. Different deductible levels can be chosen separately for each class of insurance. In this case too, one of the main features is a no claims discount of up to 40 percent. The comprehensive, clear premium calculator, which has been completely revised, also makes the sales and advisory process easier.

The high quality of the services is reflected in the numerous awards and seals of approval received by ARAG in 2017. In a comparison of legal insurance carried out by the German Society for Consumer Studies in collaboration with the N24 television news channel in mid-2017, ARAG legal insurance came out as the winner of the test in both the overall assessment and the 'Customer service' subcategory. In a survey carried out by Focus Money magazine, ARAG gained the distinction of 'fairest legal insurance provider' and received a rating of 'very good' in the middle of the reporting year. The service provided by ARAG also received top marks in a number of follow-up certification processes carried out by TÜV Saarland. A rating of 'very good' was received twice around the middle of the year under review: firstly for inhouse mediation at ARAG Service Center GmbH and in the second instance for ARAG Legal Service at ARAG SE.

The Company also performed impressively in international markets in 2017 via its branches, subsidiaries, and equity investments thanks to numerous innovative, beneficial product and service ideas.

For example, ARAG Belgium launched a new legal insurance policy for the self-employed and micro-businesses without employees in the year under review. The cover provided includes copyright infringements and identity theft. ARAG Belgium also restruc-

tured its legal insurance product for small and medium-sized enterprises and included a number of new types of cover.

ARAG SE's Norwegian subsidiary, HELP Forsikring AS, gained a new strategic partner in 2017 in the form of Dipper, the country's largest telephone company. Dipper will now offer HELP legal insurance, which includes contractual and employment legal insurance, as an additional benefit for businesses with up to 15 employees. HELP Forsikring AS has also developed special legal insurance for landlords; this will be sold in collaboration with two major Norwegian companies. In another development going forward, customers of Norwegian telecoms provider Talkmore will be able to take out special HELP legal insurance against identity theft on an individual basis when they enter into a Talkmore contract.

HELP Forsikring Filial, the Danish branch of the Norwegian subsidiary HELP Forsikring AS, entered into an alliance with Danish cellphone provider 'Call me' in the reporting year. 'Call me' offers its customers WebHELP as an integral part of its cellphone agreements.

In March 2017, HELP Försäkring Filial in Sweden, likewise a branch of the subsidiary HELP Forsikring AS in Oslo, entered into an alliance with the company 'My Safety', a specialist in the deletion of unwanted web content. HELP Försäkring Filial offers customers of My Safety an add-on in the form of special legal insurance covering criminal investigations.

In May 2017, ARAG UK introduced Care Providers' Legal Solutions in the UK market, a new innovative product aimed at the care industry. The new legal insurance policy is tailored to the specific needs of this sector. It provides bespoke cover for care home operators and care industry service providers, who are increasingly exposed to legal and regulatory risks. The UK subsidiary of ARAG SE also entered into a new collaborative partnership with Neos, an insurtech business offering smart home solutions controlled via an app. The new technology identifies fire, break-ins, or water damage and reports the incidents in real time to the customer's smartphone. An ARAG special service package and legal insurance are included to provide a comprehensive product.

In 2017, ARAG Greece also launched a similarly innovative, highly topical product solution that provides special legal insurance for the owners of unmanned drones to cover potential legal disputes.

ARAG Services Corporation, the ARAG Group's Canadian subsidiary established in 2015, has set up a new collaborative partnership with broker Benson Kearly in which ARAG legal insurance is provided as mandatory add-on cover to Benson Kearly's special liability product. This product is aimed at the managers of apartment blocks. In 2017, ARAG Services Corporation also developed legal insurance specifically tailored for various police organizations and associations.

Employees, employee skills and qualifications ARAG SE 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 2017, ARAG SE had a total of 1,121 (December 31, 2016: 1,096) employees in Germany. A further 1,511 (December 31, 2016: 1,468) 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, specialist training sessions, and e-learning. The content is wide-ranging and includes executive programs covering leadership and management, seminars on personal development, project management training, coaching, and foreign languages. All planned and completed CPD has been centrally recorded in ARAG IQ since 2016. From 2018, the CPD requirements resulting from the provisions in the new Insurance Distribution Directive (IDD) will also be recorded and monitored using ARAG IQ.

A further key component in ARAG's strategy for retaining suitably qualified employees in the Group is ARAG myCareer, an inhouse 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. With a view to systematically expanding this integration and embedding it in the Group, 20 management events around the theme of the business significance and impact of Solvency II were held in 2017 with the involvement of the top three management levels in all companies and branches. ARAG's sales academy ensures that continuous, high-quality skills development is provided for ARAG partners in the Field Sales force of ARAG Core Sales. The academy 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 (ARAG Essentials 2.0) for the corporate guidelines of the ARAG Group, which was then introduced in March 2015.

The communications process included discussions throughout the Group, the publication of an ARAG Essentials online tool at www.ARAG.com, and the creation of a values mentoring scheme. The online tool is available to all users around the clock and in all Group languages through the Group website. Users can access information on the ARAG Essentials and on the Group's locations in a fun, virtual environment. The tool is regularly updated and includes the details of any new local subsidiaries.

In each month since 2015, three out of a total of around 100 domestic and international managers at the first management level have taken on the role of mentor in the values mentoring scheme. The scheme ran until December 2017. The associated activities were published on the groupwide intranet.

The scheme covered three main areas: team campaigns aimed at bringing about positive changes in operating processes, leading to long-term improvements; mentoring aimed at optimizing individual teams' collaboration; and mentoring focusing on the social responsibility of teams outside the business, likewise with a positive impact on team development.

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. These projects both reinforce the ARAG Essentials values and contribute to the associated activity – in the form of customer focus, expertise, and efficiency. 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 Company'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.

The GDV code of conduct provides for a mandatory audit to be carried out by an independent auditor every two years. All ARAG companies in Germany underwent both an initial audit in 2015 and a subsequent audit in 2017, and emerged successfully from both audits, which were conducted in the form of an appropriateness test. The description of the compliance management system used as the basis for the audit and the positive audit report issued by the independent auditors PricewaterhouseCoopers have been published 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 audit report demonstrates that ARAG insurance companies are appropriately implementing the challenging requirements in the code in terms of quality of advice, product development, and sales management, and have successfully and sustainably put the code's main core objectives into practice in the companies' compliance and sales organization.

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.

The provisions of the EU's Insurance Distribution Directive (IDD) were implemented in the Company on schedule on February 23, 2018. The IDD aims to strengthen consumer protection and create a level playing field for all those involved in insurance sales and distribution. The areas covered by the new regulations include remuneration systems, skills, qualifications, and CPD requirements for employees in both field sales and sales administration, and additional requirements for advisory and documentation processes. The new EU Directive provides ARAG with the opportunity to achieve further improvements in quality and ensure that activities are consistently centered on the interests of the customer. This means that the focus is on sales and on the insurance product itself – starting from product development (plus the requirements for product information) through to customer contact and the settlement of claims.

The ARAG Group has done the groundwork over the last few years, although this has not been limited just to its holistic advisory approach in ARAG Core Sales and the adoption of the GDV code of conduct. Uniform standards have been rolled out for all the German companies, enabling ARAG to implement the IDD requirements on time.

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.

The personal health of employees is at the core of the first pillar of ARAGcare. The tried-and-tested components include health checks, diverse company sports activities, regular preventive medical services, and health courses. ARAG also operates a return-to-work and disability management system to ensure that the statutory requirements are implemented professionally. External specialists are regularly brought in to make sure that the individuals concerned are provided with the best possible support.

In the year under review, greater emphasis was also given to the second pillar of ARAG-care: work/life balance. ARAG once again received certification in this regard in 2017. What is officially referred to as re-auditing is in fact, as far as the Company is concerned, both a distinction and a voluntary commitment. Certification from berufundfamilie Service GmbH, an initiative of the not-for-profit Hertie foundation, is a demanding, multi-stage process. ARAG was first audited in June 2014. Subsequent certification during the late summer of 2017 involved a detailed analysis of the current position and of the further development of an HR policy that takes into account family requirements and stage of life. Following comprehensive evaluation activities, new targets were agreed, together with mandatory measures that ARAG will implement by 2020. These measures include, for example, overall management with an increase in the proportion of women in management positions and changes to make the arrangements for working hours and working location even more flexible. There will also be a focus on improving information and communication in relation to work/life balance issues and sabbatical leave for employees.

For the eighth time, ARAG received a seal of approval in the Corporate Health Awards 2017 based on its comprehensive offering covering occupational health management and work/life balance.

Targets for the proportion of women in management functions In accordance with the provisions in the German Act on the Equal Participation of Women and Men in Managerial Positions (FührposGleichberG), the Company must set targets for the proportion of women at the two management levels below the Management Board, on the Management Board itself and on the Supervisory Board, and must also determine appropriate deadlines for achieving the targets. The Management Board advocates a rising proportion of women in managerial positions, especially as long as the proportion remains below 30 percent. To this end, numerous supporting measures are being implemented as part of the work/life balance project. The Management Board had set a target for the proportion of women at the first management level below the Management Board of 11 percent and a target at the second management level of 25 percent, in both cases to be achieved by June 30, 2017. Both targets represented an increase compared with the situation at the time the targets were set. The Supervisory Board had set the following targets for June 30, 2017 in respect of the proportion of women: 11 percent on the Supervisory Board and 0 percent on the Management Board.

At the first management level below the Management Board, the actual proportion as of June 13, 2017 was 10 percent. At the second management level, the target was comfortably exceeded with a proportion of 30 percent. The actual proportions for the Supervisory Board and the Management Board were the same as the targets, i.e. 11 percent and 0 percent respectively.

For the next target attainment deadline of June 30, 2019, the Management Board has set a target for the proportion of women at the first management level below the Management Board of 11 percent and a target at the second management level of 30 percent. Both targets represent an increase compared with the situation at the time the targets were set. The Supervisory Board has decided on the following targets for June 30, 2019 in respect of the proportion of women: 11 percent on the Supervisory Board and 0 percent on the Management Board. These two targets are the same as the actual percentages at the time the targets were set.

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 four training cycles so far, a total of 316 teachers, specialists in educational social work, and parents from 96 high schools and vocational colleges in different school districts across the state have taken part. The project is currently running at twelve 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).

Since September 2016, ARAG has been a sponsor of MediationsZentrale München e.V. The school mediation team at this not-for-profit organization regularly sends out professionally trained mediators to public sector and private schools in the Greater Munich area to act as impartial points of contact for all conflicts and problems arising in day-to-day school activities.

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 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.

In 2017, ARAG therefore focused more intensely on protecting online privacy rights. At the instigation of ARAG, a joint research project was launched in cooperation with the Research Center for IT Law and Social Networks Policy at the University of Passau. The project involved developing an alternative to the contentious Enforcement of Rights on Social Networks Act (NetzDG) in Germany. The results were published on Safer Internet Day at the beginning of February 2018.

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. Schools throughout Germany are faced with the challenge presented by the digital transformation. At the same time, digitalization opens up numer-

ous opportunities for school-based education. ARAG and DKJS therefore launched a joint program in November 2017 referred to as 'bildung.digital' (digital education). This program helps schools to develop digital education strategies and ensure that the strategies become firmly established as part of their activities. Some 40 (full) day schools from eight federal states have committed to using four cross-state networks in the program via the portal 'bildung.digital-Netzwerk ganztägig bilden'.

Equal opportunities is also the theme of the 'Kickwinkel' project in Düsseldorf, which ARAG initiated and supports on an ongoing basis together with other local partners. 'Kickwinkel' is an integration project based on football for unaccompanied male refugees from Iraq, Afghanistan, Somalia, Eritrea, Gambia, Guinea, and Iran. The project enables 20 young people to train at a Düsseldorf club twice a week. A tournament with teams from all the project partners was held in July 2017, demonstrating yet again that 'sport unites'.

Non-financial statement for the Group

As a result of the provisions in the German CSR Directive Implementation Act (CSR-RUG), ARAG SE has been subject to a non-financial reporting obligation since 2017 in accordance with section 341 a (1a) HGB. As ARAG SE is included in the non-financial statement for the Group issued by its parent company ARAG Holding SE, Düsseldorf, ARAG SE has elected to exercise the exemption option under section 341 a (1a) sentence 3 in conjunction with section 289 b (2) HGB. The exempting non-financial statement for the Group issued by ARAG Holding SE is publicly accessible in German at www.arag.com/german/press/publications/

This is complemented by the detailed reporting in ARAG's 2017 Sustainability Report.*

Solvency

Under section 89 (1) VAG, all insurance companies are obliged to have eligible own funds available at all times that, as a minimum, are sufficient to satisfy the solvency capital requirement. The Solvency II rules came into force on January 1, 2016. In accordance with section 40 VAG, a solvency and financial condition report* must be published no later than 14 weeks after the end of the financial year. This report must explain the solvency position in a manner that is understandable to the general reader. Insurance groups must also ensure at group level that the solvency margin is covered by eligible own funds and that these funds are appropriately allocated in the group. Evidence of compliance with the solvency requirements is submitted to the German Federal Financial Supervisory Authority (BaFin) on a quarterly basis.

Solvency ratios must be calculated quarterly at the level of the insurance company and at group level.

In the year under review, ARAG SE ensured that it covered the statutory requirement for the solvency margin in accordance with current solvency regulations at all times.

* Not part of the management report.

III. Dependent Company Report

ARAG Holding SE, Düsseldorf, indirectly holds a majority interest in ARAG SE. The existence of the majority interest was notified to ARAG Allgemeine Rechtsschutz-Versicherungs-AG (now ARAG SE) on April 28, 2000 by the Management Board of ARAG AG (now ARAG Holding SE) in accordance with section 20 (1) and (4) of the German Stock Corporation Act (AktG).

ARAG SE is therefore a dependent company within the meaning of section 17 (1) AktG in relation to ARAG Holding SE.

The report on relationships with affiliated companies pursuant to section 312 AktG concludes with the following declaration:

“In accordance with the circumstances known to us at the time the legal transactions were undertaken or the activities were carried out or omitted, our Company received an appropriate consideration for each legal transaction. Other than the activities listed, the Company did not carry out or omit any other reportable activities. Our Company did not incur any disadvantage from the activities carried out at the instigation of or in the interests of the controlling entity or its affiliated companies.”

IV. Outlook, Opportunity and Risk Reports

Outlook

Future global economic growth remains subject to many significant risks. Besides the risk of a sudden fall in growth in individual economies around the globe, these risks include a potential increase in protectionist trends as well as political risks, especially in Europe. In the case of the latter, the most notable danger is the possibility of a disorderly hard Brexit resulting from a lack of progress in the negotiations on the UK's withdrawal from the EU. However, a potential deterioration of the conflict in Catalonia and new political scenarios arising from elections in 2018 could also jeopardize stability in Europe.

Furthermore, it is possible that the low interest rates could contribute to excesses in the financial system. For example, there is a risk of misallocations caused by a distortion of market prices. In addition, the risk of financial market turmoil arising in the wake of the forthcoming shift away from the long-standing policy of low interest rates pursued by many central banks should not be discounted. This shift is only happening very slowly at the moment, if at all. At present, consumer price inflation is at a modest level, but this could change in view of the current monetary environment and rising capacity utilization. Central banks could then be forced into an unexpectedly rapid rise in interest rates. Another factor is that global indebtedness has continued to grow since the financial crisis and is now at a record level. While public sector indebtedness in the industrialized economies has continued to rise, the volume of lending to households and businesses as a proportion of GDP has retreated a little in recent years.

Political developments in Europe demand particular attention. One major concern is that the future political and economic relationships between the UK and the EU have not yet been clarified. So far, the vote for Brexit has not had any substantial adverse effects on the real economy. This indicates a prevailing expectation that the parties will find a solution limiting the damage to the economy. However, given the progress in the negotiations to date, it is not at all clear whether an agreement can be reached by the spring of 2019. If the negotiations fail, a hard Brexit would have a negative economic impact, primarily on the UK, but also to a lesser extent on its European trading partners. It is unlikely that this would lead to any serious adverse consequences for the global economy. However, Europe's political risks are not restricted just to the uncertainty surrounding Brexit. In many EU member states, parties on the fringes of the political spectrum are enjoying a surge in popularity. If surveys are to be believed, support for parties critical of the EU and/or the euro is at a very high level. The recent developments in Catalonia underline the political tensions that continue to prevail. Forthcoming elections in some European countries will also bring additional risks. A situation that reignites the crisis in the eurozone can therefore not be fully ruled out.

On the other side of the equation, however, there are numerous opportunities and a great deal of potential for stronger growth in the global economy. An unexpectedly sharp increase in capital spending, predominantly in the eurozone, could push up the rate of expansion markedly. A more expansionary fiscal policy in the US could provide an additional stimulus not currently factored into the forecasts. Overall, the German Council of Economic Experts anticipates that growth will continue, both globally and in Europe. For 2018, it is forecasting a rise in global economic output of around 3.2 percent and an increase in eurozone GDP of 2.1 percent.

In Germany, the economic recovery is now in its fifth year. Capacity utilization is higher than usual. The rapid growth means the country is fast approaching an economic boom, increasing the risk of overheating. Higher inflation rates compared with recent years will also have a dampening effect on wage growth in real terms. However, the forecasts do not show any dip in the uptrend in consumer spending in the future. Consumer sentiment remains very favorable, bolstered by the stability in the labor market; willingness to spend and income expectations are still positive. Nevertheless, consumer price inflation is projected to rise slightly over the forecast period. Again in 2018, household consumption will remain the primary driver behind the country's economic growth, making a substantial contribution to the increase in the nation's GDP. The number of people in employment is predicted to rise once again by around 500,000 in 2018; current forecasts project that there will be 32.7 million people in employment subject to social security contributions and 4.7 million in exclusively marginal employment (jobs with very low earnings).

In all probability, however, it will not be possible to maintain the current pace of growth at quite the same level in 2018. Nevertheless, because of the significant carryover from 2017, the Council of Economic Experts is predicting an average GDP growth rate for the year of 2.2 percent.

The excellent economic situation offers an opportunity to focus on the future challenges as part of a potential readjustment in economic policy. These challenges include, notably, demographic change and digitalization.

Demographic change will cause the size of the available workforce to shrink. A shortage of specialists is already evident in some sectors of the economy. It will therefore become increasingly critical to make better use of the available workforce potential and improve employee retention. This could trigger the need for measures related to work/life balance, such as the further expansion of childcare facilities, and immigration legislation. Politicians should also focus their attention on reducing long-term unemployment and integrating genuine asylum seekers into the job market.

The digitalization of the economy and society is leading to a comprehensive structural transformation, which politicians should make every effort to facilitate, for instance through innovation-friendly regulation, the systematic digitalization of government administrative activities, and measures to ensure that the labor market is flexible. In addition, education and training needs to be enhanced so that employees are more adaptable to the new requirements in the digital working environment. Digitalization is the basis for the great hope that it will be possible to achieve increases in labor productivity in the

future. Greater connectivity between players, the associated improvements in the provision and use of information, and the growing maturity of autonomous systems hold out the prospect of increasing the efficiency of production processes and enhancing product quality. These changes also mean that business models and service delivery processes can be modified so that they have a greater focus on the needs and wishes of consumers.

The insurance industry is being heavily impacted by the trends described above. One of the factors taken into account in the latest forecasts of the 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, examples of other action priorities include the increasing differentiation between customer groups and, as described above, 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 the pluralization of sales structures) are far-reaching.

Furthermore, digitalization – one of the major challenges going forward – is stepping up the pressure and the speed of change in the rather conservative insurance industry. There is a need to open up additional new sales, service, and communication channels with a focus on consumers. However, because the market is not made up solely of online customers, development is not concentrated on ‘either-or’ concepts or short-term solutions, which would not satisfy customer wishes. 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 easy, barrier-free access to smart insurance benefits and services. Online business models will therefore soon no longer be aimed at particularly price-sensitive customers but will have to become an integral component – configured for maximum ease of use – in the range of services provided by each and every insurance company.

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. However, demand for insurance services is currently being positively impacted by the very favorable financial position enjoyed by consumers on the back of the beneficial situation in the German job market.

As a consequence, premium income in the insurance industry is expected to continue to grow. The GDV is forecasting an increase of approximately 1.3 percent for the German market in 2018 (2017: 1.3 percent). 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 3.0 percent in 2018 (2017: 2.9 percent). Rising sums insured and extensions of the cover could once again be the growth drivers in the private property insurance segment, leading to an increase in the premium

income generated by this segment of up to 4.0 percent (2017: 4.5 percent). In the case of legal insurance, the GDV again predicts a rise in premiums of around 4.0 percent (2017: 4.0 percent) in view of a number of factors, notably the opportunities to adjust premiums.

In the year under review, ARAG SE maintained its sound level of performance in line with the forecasts made in the previous year. However, the projected premium income increase of approximately 3 percent was well exceeded by the actual figure of 5.5 percent. The proportion of the gross premiums written accounted for by international business remained at 59.9 percent. In contrast to the prior-year forecast, the claims ratio rose by 2.3 percentage points due to higher accumulation risk in the legal insurance business and extensive use by policyholders in the Netherlands of the right to choose their own attorneys. Absolute costs rose in the reporting year as expected, but the cost ratio remained steady year on year because of the significant increase in premiums. In line with forecasts, the underwriting result was positive, but lower than in 2016. In 2016, it had not been possible to prepare a rationally argued forecast for gains and losses on investments because of the surprising outcome of the US presidential elections and the ECB's monetary policy. Fears of a contraction turned out to be unfounded as income from equity investments rose sharply. At €56,790.6 thousand, profit before tax was lower than in 2016 (€68,027.5 thousand), as anticipated. The net retained profit of €32,031.2 thousand exceeded the forecast by some way.

The performance of ARAG SE will remain on a growth trajectory in the current year. The Solvency II regulatory regime specifies tight deadlines as well as the scope and frequency of reports to the insurance supervisor and to the public, as a result of which relevant administrative processes must be optimized. ARAG SE has prepared its operational structures for these requirements. In addition, the use of a partial internal model allows the relatively homogeneous legal insurance business to be taken into consideration on a Company-specific basis when determining the capital requirement. The flexibility that this creates will be used to specifically develop further new international growth markets and acquire portfolios.

Premiums written are projected to grow by approximately 2.5 percent on the back of the above combined with the development of innovative legal insurance cover in Germany, the expansion of the portfolio of services in connection with other insurance related to legal insurance and insurance-related activities, and new digital offerings. In terms of claims, it is anticipated that there will be some easing again in 2018 following adjustments in 2017 because of accumulation risk and expected cost increases in the settlement of claims in markets outside Germany. The claims ratio is predicted to be at the level of 2016, i.e. just under 53 percent. The costs side of the equation will be affected by further investment in the digitalization of business processes and services. However, the cost ratio will remain unchanged because of the growth generated. Overall, the underwriting result for 2018 is projected to be at the level of the reporting year.

It is not anticipated that the ECB will move away from its expansionary monetary policy in 2018, even though US interest-rate hikes are likely. Current volatility in equity markets could be an indicator of a forthcoming increase in interest rates or simply be a short-term correction. It is difficult to make a forecast of gains and losses on investments in these circumstances. Overall, it is predicted that the current year will see slightly lower gains on investments than in the year under review because the potential for further reversals of write-downs has been exhausted.

No further charges will arise at ARAG SE – in respect of the year under review or in the future – from the life insurance business sold in 2017. After taking into account the opportunities and risks, the profit before tax for 2018 is projected to be lower than that generated in the year under review.

Opportunity report

ARAG SE, as a legal insurance provider with subsidiaries that operate property and health insurance business, is considerably better positioned in terms of efficiency and competitiveness compared with 2016. By specifically focusing on the health and property insurance business – including the very successful legal insurance business in Germany and in many international markets – the Company has been able to reduce business risk substantially. Based on this realignment, ARAG has responded to the challenges presented by the low interest rates and has answered, as far as its own business is concerned, one of the critical questions in the insurance industry. In the meantime, the customers have not been forgotten despite the associated reorganization of the business: In the year under review, group premiums increased by almost €70,000.0 thousand. ARAG SE, in combination with its international branches, enjoys unique competitive advantages.

At the moment, the insurance industry is already facing another critical issue, namely the digital transformation. ARAG now has to respond to this challenge just as assiduously. Both in Germany and abroad, a whole plethora of innovative, beneficial digitalization ideas have recently been implemented. Nevertheless, there is still huge potential for the exploitation of innovation arising from digitalization – in terms of processes, products, sales, and above all in terms of cutting-edge, needs-based services for customers. Online business is already making a substantial contribution to growth: At the end of the year under review, 11 percent of the customer portfolio in Germany had already been derived from this sales channel.

Over the short to medium term, digital technologies will lead to a fundamental change in consumer behavior. The insurance industry therefore has to provide solutions that help the customer quickly and without fuss. For the same reason, it is also beyond doubt that, in the area of legal services and legal advice, a focus solely on traditional insurance products is no longer the way forward. The boundaries in the industry will become blurred: Internet giants and specialist start-ups are already using new business models to force their way into the market.

ARAG SE sees digital transformation as a clear set of opportunities. It is taking on the related challenges with the clear aspiration of playing a pioneering role, and indeed is already doing so with the many digitalization projects and activities that it has successfully implemented to date. This applies both to Germany and to the international markets, in which suitable digitalization concepts are being developed for each of the markets concerned. Even in the context of digitalization, the basic principle that ARAG will always decide, perform, and deliver in the interests of its customers applies throughout the Group.

ARAG's Group strategy continues to provide for a distribution of responsibilities throughout the 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. ARAG's international structure is also 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 SE 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.

This two-dimensional diversification strategy in the Group is also enabling ARAG SE to move away from its original tightly focused positioning as a niche provider in Germany. A specialist insurer concentrating solely on one line of business in its portfolio is considerably more susceptible to risk. The strategic approach at ARAG is therefore to actively reduce risk and is based on spreading risk evenly across all markets and segments.

To manage the international structure of ARAG SE, 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 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 business 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.

ARAG SE will work systematically and energetically to meet the challenges presented by the markets. In direct implementation of the Group strategy, ARAG SE will continue the process of international diversification and significantly expand the international share of the business.

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 the 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 business strategy, the Management Board specifies the risk strategy and defines the capital adequacy requirements and the required limits for the Company. 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 Company 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 exposure 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.

Groupwide risk standards are applied to ensure a consistent and appropriate procedure is used in risk modeling, performance measurement, and in the use of relevant risk parameters in the calculations.

Risk management The Company'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 Company 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 Company. 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. It also ensures 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 is an instrument of the 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 operational 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 findings.

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 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. Likewise, catastrophe and accumulation risk is assessed by simulating losses that may arise from 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>
2017	57.1	53.4	2.8
2016	57.7	51.2	4.6
2015	61.0	52.5	5.6
2014	61.7	55.8	3.7
2013	63.8	58.6	3.3
2012	60.0	55.4	3.0
2011	68.3	56.1	3.9
2010	68.6	63.6	2.8
2009	71.7	64.8	3.8
2008	66.5	58.3	4.6

At operational level, underwriting risk arising from legal insurance is managed by means of underwriting, premium, 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 in the insurance business largely arises in connection with receivables from reinsurers, receivables from policyholders, and receivables from insurance brokers. It 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 partial internal model. The method used to bring together the different types of exposure, aggregate them, and determine the associated correlations is specified in the model.

The risk of default on receivables from reinsurers is measured on the basis of the information available and proportionality considerations. The reinsurers' individual credit ratings are explicitly used. Default risk in connection with reinsurance treaties 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 €3,956.5 thousand (December 31, 2016: €12,436.2 thousand). As of December 31, 2017, the average default rate over the last three years for these receivables in respect of the headquarters in Germany was 25.1 percent (December 31, 2016: 25.6 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 ARAG SE's fixed-income securities by €73.5 million.
- 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 €35.3 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.
- Migration/default risk: rating level changes or changes in the extent of projected defaults. The breakdown of interest-bearing investments by rating is as follows:

Fixed-income securities by rating class

(Proportion (%) by fair value)

AAA	17.5
AA	14.0
A	29.8
BBB	34.4
BB	3.0
B	1.3
CCC	0.0
CC	0.0
C	0.0
D	0.0
Not rated	0.0

The breakdown of fixed-income securities is as follows (fair values): of the fixed-income securities – including securities held indirectly through institutional funds – approximately 35.3 percent are accounted for by financial services entities, 26.3 percent by public-sector bonds, and 38.3 percent by corporate bonds.

- 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 an internal model. An economic scenario generator is used to simulate capital market scenarios looking at interest rates, share prices, real estate prices, credit spreads, credit ratings/defaults, and exchange rates. These risk factors are used to determine the possible fair values of investments in one year's time. The market risk itself results from the 1 in 200 year event considering all risk factors simultaneously, 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 ARAG SE (short selling) are not permitted.

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 or liquidity shortfall is calculated on a rolling basis.

Each line item on the balance sheet is assigned to a liquidity class so that the liquidity of the investment 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 Company 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. It also includes losses from cyber risk. In addition, operational risk encompasses legal risk but does not include reputational risk or risks arising from strategic decisions.

The Company 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. With regard to cyber risk, these measures include information technology security measures and insurance solutions. Additional measures have been taken to counter the potential impact from a cyberattack. These include, for example, appropriate countermeasures in a business continuity management system.

Overall risk position

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 Company. The overall risk position does not currently point to any trends in 2018 that could jeopardize the continued existence of the Company as a going concern or cause a significant negative impact on net assets, financial position, or results of operations.

Risk position The regulatory minimum capital requirement in accordance with VAG provisions is met in full. Moreover, the eligible own funds are significantly higher than the solvency capital requirements calculated in accordance with VAG. Further details of the coverage situation can be found in the solvency and financial condition report*.

* Not part of the management report.

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Balance Sheet as of December 31, 2017

Assets

(€)

A. 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.	Equity investments
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 of which in respect of affiliated companies: € 3,675,000.00 (Dec. 31, 2016: € 3,975,000.00)
4.	Miscellaneous lending
a)	Registered bonds
b)	Promissory notes and loans
c)	Sundry lending
5.	Bank deposits
6.	Other investments
IV.	Deposits with ceding insurers

C. Receivables

I.	Receivables from direct insurance business
1.	from policyholders
2.	from insurance brokers
	of which from affiliated companies: € 26,950.14 (Dec. 31, 2016: € 133,422.85)
II.	Receivables from reinsurance business
	of which from affiliated companies: € 299,490.57 (Dec. 31, 2016: € 292,265.28)
III.	Miscellaneous receivables
	of which from affiliated companies: € 3,957,434.38 (Dec. 31, 2016: € 5,773,217.53)
	of which from other long-term investees and investors: € 231,393.78 (Dec. 31, 2016: € 16,565.62)

D. Miscellaneous assets

I.	Property and equipment and inventories
II.	Current bank balances, checks and cash on hand
III.	Other assets

E. Prepaid expenses and accrued income

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

F. Deferred tax assets

G. Excess of plan assets over pension liabilities

Total assets

				Dec. 31, 2017	Dec. 31, 2016
				7,658,413.63	8,329,472.13
			93,557,587.84		97,563,670.52
		273,016,708.28			225,017,698.96
		0.00			1,655,527.11
		16,887,569.37			16,887,569.37
			289,904,277.65		243,560,795.44
		617,622,846.16			625,493,318.99
		396,850,198.80			301,550,383.27
		9,179,927.98			3,975,000.00
	140,511,291.88				140,511,291.88
	251,959,862.44				243,995,110.85
	79,078.08				150,107.42
		392,550,232.40			384,656,510.15
		57,968,966.00			98,570,813.32
		4,535,534.31			5,331,278.41
			1,478,707,705.65		1,419,577,304.14
			49,676,929.50		44,388,849.23
				1,911,846,500.64	1,805,090,619.33
		27,443,545.84			25,974,932.12
		17,998,834.22			19,854,540.66
			45,442,380.06		45,829,472.78
			46,740,155.11		44,836,329.39
			8,066,930.76		10,461,382.14
				100,249,465.93	101,127,184.31
			15,330,876.20		16,320,490.85
			58,303,479.05		67,912,841.66
			23,290,583.17		38,128,341.36
				96,924,938.42	122,361,673.87
			7,400,196.42		7,260,642.26
			2,050,228.36		2,240,502.16
				9,450,424.78	9,501,144.42
				0.00	6,080,380.79
				0.00	0.00
				2,126,129,743.40	2,052,490,474.85

Balance Sheet as of December 31, 2017

Equity and liabilities

(€)

A. Equity

- I. Subscribed capital
- II. Capital reserve
- III. Revenue reserves
 - 1. Statutory reserves
 - 2. Other revenue reserves
- IV. Net retained profit

B. Subordinated liabilities

C. Technical provisions

- I. Unearned premiums
 - 1. Gross amount
 - 2. less: portion for outward reinsurance business
- II. Provision for outstanding claims
 - 1. Gross amount
 - 2. less: portion for outward reinsurance business

III. Equalization provision and similar provisions

IV. Miscellaneous technical provisions

D. Other provisions

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

E. Deposits received from reinsurers

F. Other liabilities

- I. Liabilities from direct insurance business
 - 1. to policyholders
 - 2. to insurance brokers
 - of which to affiliated companies: €38,604.22 (Dec. 31, 2016: €16,281.97)
 - of which to other long-term investees and investors: €47.89 (Dec. 31, 2016: €48.65)
- II. Liabilities from reinsurance business
 - of which to affiliated companies: €95,657.16 (Dec. 31, 2016: €90,160.50)
- III. Liabilities to banks
- IV. Miscellaneous liabilities
 - of which tax liabilities: €18,842,528.53 (Dec. 31, 2016: €14,419,570.00)
 - of which social security liabilities: €1,765,107.33 (Dec. 31, 2016: €1,759,752.31)
 - of which to affiliated companies: €18,017,463.12 (Dec. 31, 2016: €16,129,957.34)
 - of which to other long-term investees and investors: €0.00 (Dec. 31, 2016: €0.00)

G. Deferred income and accrued expenses

H. Deferred tax liabilities

Total equity and liabilities

			Dec. 31, 2017	Dec. 31, 2016
		100,000,000.00		100,000,000.00
		81,772,569.19		81,772,569.19
	10,000,000.00			10,000,000.00
	215,600,000.00			198,900,000.00
		225,600,000.00		208,900,000.00
		32,032,184.31		31,701,021.52
			439,404,753.50	422,373,590.71
			30,000,000.00	30,000,000.00
	200,629,038.37			200,249,508.90
	1,417,577.35			1,417,577.35
		199,211,461.02		198,831,931.55
	1,102,456,262.53			1,062,854,310.12
	2,567,850.21			1,784,031.80
		1,099,888,412.32		1,061,070,278.32
		16,873,047.50		13,794,281.00
		690,000.00		882,000.00
			1,316,662,920.84	1,274,578,490.87
		172,270,708.69		164,314,789.76
		18,260,905.42		12,938,359.11
		63,071,289.08		65,207,692.91
			253,602,903.19	242,460,841.78
			1,458,215.89	1,509,590.45
	9,181,718.98			10,593,565.54
	24,697,402.32			24,855,693.40
		33,879,121.30		35,449,258.94
		2,135,769.00		1,878,744.58
		0.00		0.00
		48,835,347.02		44,022,550.43
			84,850,237.32	81,350,553.95
			140,178.49	217,407.09
			10,534.17	0.00
			2,126,129,743.40	2,052,490,474.85

Income Statement for the Period from January 1 to December 31, 2017

(€)

I. Underwriting account

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. Miscellaneous underwriting income for own account
3. 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
4. Change in miscellaneous net technical provisions
5. Own account insurance business operating expenses
a) Gross insurance business operating expenses
b) less: commissions received and profit sharing received from outward reinsurance business
6. Miscellaneous underwriting expenses for own account
7. Subtotal
8. Change in the equalization provision and similar provisions
9. Underwriting result for own account
Carried forward:

			2017	2016
	870,004,120.46			824,615,978.15
	-1,201,294.40			-5,247,633.53
		868,802,826.06		819,368,344.62
	-761,425.27			-5,334,530.43
	0.00			218,467.35
		-761,425.27		-5,116,063.08
			868,041,400.79	814,252,281.54
			1,683,218.94	1,464,471.83
	423,876,206.67			409,338,599.15
	-1,704,250.90			-855,825.29
		422,171,955.77		408,482,773.86
	-41,357,688.74			-7,543,653.05
	783,818.41			633,419.19
		-40,573,870.33		-6,910,233.86
			462,745,826.10	415,393,007.72
			192,000.00	-6,000.00
		389,482,522.93		366,974,892.54
		-301,993.32		-2,590,163.97
			389,180,529.61	364,384,728.57
			70,803.73	0.00
			17,919,460.29	35,933,017.08
			-3,078,766.50	-5,556,401.00
			14,840,693.79	30,376,616.08
			14,840,693.79	30,376,616.08

Income Statement for the Period from January 1 to December 31, 2017

(€)

Brought forward:

II. Non-underwriting account

1. Income from investments

a) Income from equity investments

of which from affiliated companies: € 14,908,374.67 (2016: € 11,185,074.66)

b) Income from other investments

of which from affiliated companies: € 1,695,210.96 (2016: € 2,154,166.06)

aa) Income from land, land rights and buildings, including buildings
on third-party land

bb) Income from other investments

c) Income from reversals of write-downs

d) Gains on the disposal of investments

e) Income from profit-pooling, profit-transfer and partial profit-transfer agreements

2. Expenses for investments

a) Expenses for the management of investments, interest expense and similar charges and
miscellaneous expenses for investments

b) Depreciation, amortization and write-downs of investments

of which write-downs: € 4,638,237.27 (2016: € 6,220,062.95)

c) Losses on the disposal of investments

3. Other income

4. Other expenses

Non-underwriting result**5. Profit/loss from ordinary activities**

6. Extraordinary income

7. Extraordinary expenses

8. Net extraordinary income/expense

9. Income taxes

of which deferred taxes: € 6,090,914.96 (2016: € 23,655,894.04)

10. Miscellaneous taxes

11. Net income for the year

12. Profit brought forward from 2016

13. Appropriation to revenue reserves

a) To statutory reserves

b) To other revenue reserves

14. Net retained profit

				2017	2016
				14,840,693.79	30,376,616.08
		21,308,052.17			14,546,427.63
	6,089,403.48				6,382,303.57
	35,004,769.34				33,791,899.85
		41,094,172.82			40,174,203.42
		4,086,698.73			8,939,317.40
		1,535,620.08			8,848,945.81
		17,964,357.02			14,019,208.11
			85,988,900.82		86,528,102.37
		6,769,009.52			6,310,460.61
		5,604,752.76			7,250,941.94
		599,281.48			288,072.32
			12,973,043.76		13,849,474.87
				73,015,857.06	72,678,627.50
			98,133,834.46		89,919,753.75
			129,199,745.95		124,947,450.69
				-31,065,911.49	-35,027,696.94
				41,949,945.57	37,650,930.56
				56,790,639.36	68,027,546.64
			0.00		0.00
			0.00		0.00
				0.00	0.00
			22,181,607.32		35,156,509.17
			2,577,869.25		1,208,499.10
				24,759,476.57	36,365,008.27
				32,031,162.79	31,662,538.37
				1,021.52	38,483.15
				0.00	0.00
				0.00	0.00
				32,032,184.31	31,701,021.52

Notes to the Financial Statements

I. General Disclosures

ARAG SE operates legal insurance and reinsurance business. Outside Germany, the insurance offering also includes cover for a variety of financial losses as well as emergency assistance insurance. The Company holds equity investments in other insurance companies and other companies pursuing a purpose that is related to the business activities of ARAG SE. ARAG SE is entered in the commercial register of the Düsseldorf local court under the number HRB 66846. Its registered office is ARAG Platz 1, 40472 Düsseldorf, Germany. The financial statements have been prepared in accordance with Book Three of the German Commercial Code (HGB), taking into account the supplementary provisions applicable to large corporations in Part Two and the supplementary provisions applicable to insurance companies in subsection 2, as well as the supplementary provisions in the Regulation on the Accounting of Insurance Undertakings (RechVersV). The Company is a large corporation within the meaning of section 267 (3) HGB. Therefore, and pursuant to the obligations under section 341a (1) HGB, the accounting rules for large corporations have been applied.

II. Disclosures on Accounting Policies

Accounting policies

Purchased **intangible assets** are carried at cost and reduced by straight-line amortization according to their estimated useful life. No internally generated intangible assets were capitalized. **Land and buildings** are valued at cost less depreciation. Write-downs of €1,473,390.08 were recognized in the year under review owing to permanent asset impairment. In the reporting year, there were no reversals of write-downs that would have been necessary if the reason for the original write-down had no longer existed. The carrying amount of land and buildings held for own use (see also chapter IV. Non-Insurance Disclosures) is determined as a proportion of the total carrying amount according to actual usage.

Investments in affiliated companies and equity investments are valued at cost, in some cases reduced by write-downs as a consequence of permanent impairment. In this regard, write-downs amounting to €391,000.00 were recognized in the reporting year. There were no reversals of write-downs pursuant to section 253 (5) HGB in 2017 because the reasons for the write-downs still applied.

The table below shows shares in affiliated companies and equity investments that are intended to serve the Company's own operations by establishing a lasting relationship; the equity and profit/loss of these companies are stated:

Shares in affiliated companies and equity investments

Name and registered office of company	Shareholding (%)	Equity (€)	Profit/loss (€)
1. Affiliated companies			
a) Insurance companies			
ARAG Allgemeine Versicherungs-AG*, Düsseldorf	100.00	55,322,905.72	17,964,357.02
ARAG Krankenversicherungs-AG, Munich	94.00	64,552,897.92	8,900,000.00
Help Forsikring AS, Oslo	100.00	27,556,379.64	3,066,588.11
b) Other companies – limited companies			
ARAG International Holding GmbH, Düsseldorf	100.00	57,684,220.21	11,528,423.07
ARAG Liegenschaftsverwaltungs- und Beratungsgesellschaft mbH, Düsseldorf	100.00	899,644.41	- 36,282.16
ARAG Service Center GmbH, Düsseldorf	80.00	394,856.75	47,650.75
ARAG IT GmbH, Düsseldorf	100.00	8,836,851.44	267,855.33
CURA Versicherungsvermittlung GmbH, Düsseldorf	100.00	980,787.52	262,352.41
Solfin GmbH, Düsseldorf	75.10	767,613.58	314,029.57
ALIN 1 Verwaltungs-GmbH, Düsseldorf	100.00	24,706.23	2,623.27
Justix GmbH, Cologne	100.00	3,533,619.43	- 2,966,380.57
ARAG plc., Bristol	100.00	12,579,746.31	1,051,799.82
ARAG-France S.A.R.L. Assistance et Reglement de Sinistres Automobiles et Generaux, Versailles	100.00	18,988.00	0.00
ARAG Legal Services B.V., Leusden	100.00	252,733.67	- 232,224.54
ARAG Scandinavia AS, Oslo	100.00	3,047.79	0.00
MIA Multiline Insurance Agency s. r. l., Verona	100.00	50,000.00	0.00
Agencia de Seguros ARAG SA, Barcelona**	100.00	375,815.65	224,669.41
ARAG Services Spain & Portugal S.L., Barcelona	100.00	456,040.81	46,843.71
c) Other companies – partnerships			
ARAG Liegenschaftsverwaltungs- und Beratungs-GmbH & Co. Immobilien KG, Düsseldorf	50.00	4,968,156.57	- 1,108,398.01
ALIN 1 GmbH & Co. KG, Düsseldorf	100.00	15,743,438.61	477,725.10
2. Associates			
AXA ARAG Rechtsschutz AG, Zurich**	29.17	46,337,536.96	13,546,746.08

* Profit before profit transfer.

** Figures from the last available financial statements (for the year ended December 31, 2016).

Equities, investment fund shares/units, and other fixed-income and variable-yield securities that have not been classified as permanent fixed assets are valued at the lower of cost or quoted market price/market value as of the reporting date in accordance with section 341 b (2) HGB in conjunction with section 253 (1), (4), and (5) HGB. In application of the strict principle of lower of cost or market value, the following write-downs were recognized in 2017: €39,568.24 (2016: €72,700.74) in respect of equities and investment fund shares/units and €1,894,253.76 (2016: €1,959,552.81) in respect of bonds. Write-downs amounting to €840,025.19 (2016: €0.00) were recognized in respect of investment fund shares/units in application of the discretionary principle of lower of cost or market value. Reversals of write-downs pursuant to section 253 (5) HGB were recognized in the year under review as follows: €90,127.74 (2016: €0.00) in relation to equities, €3,806,013.24 (2016: €5,808,696.26) in relation to investment fund shares/units, and €190,557.57 (2016: €998,765.00) in relation to bonds. As of the reporting date, undisclosed liabilities of €472,268.73 (December 31, 2016: €147,179.85) were not netted as a result of the application of the discretionary principle of lower of cost or market value.

ARAG SE made use of the option to select the discretionary principle of lower of cost or market value in accordance with section 341 b (2) second half-sentence HGB for those institutional investment fund shares/units and bearer bonds that the Management Board intends to use permanently as part of the working capital of the insurance business. Subsequent valuation of the investment fund shares/units classified as fixed assets is based on the long-term market value determined in a fund review. As of December 31, 2017, the long-term market value was assumed to be the quoted market price.

As in prior years, additions to investment fund shares/units, but not additions to bearer bonds, were recognized under fixed assets.

Registered bonds are accounted for at their nominal or redemption 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. **Promissory notes, loans and receivables secured by mortgages or land charges, and sundry lending items** are recognized at cost unless permanently impaired. No write-downs to a lower fair value were necessary in the year under review or the previous year.

Bank deposits as well as deposits with and deposits received from ceding insurers are recognized at their nominal amount. Increases and decreases in bank deposits are only netted where the credit balances are held by the same business unit. **Other investments** comprise shares/units in infrastructure funds and private equity funds. They are valued at cost. The fair value as of the reporting date is reviewed on the basis of the net asset values reported by the fund management companies. No write-downs pursuant to section 253 (3) sentence 5 HGB have been necessary to date.

Investments are individually assigned to the business units (headquarters and branches). The assignment is documented by recording the investments in the relevant books of the business unit concerned. Income from investments is allocated to each business unit

according to the assignment of the investment in question. Assignments are reviewed annually using the modified capital allocation approach determined by the German tax authorities – which has been approved by the Organisation for Economic Co-operation and Development (OECD) – and adjusted by means of compensatory payments.

Deposits with ceding insurers are recognized at the nominal value of the collateral furnished to cedants. The residual maturity is less than one year because the contracts are renewed annually.

Receivables are generally recognized at their nominal amount. A general allowance for latent credit risk is deducted from **receivables from policyholders** after specific allowances have been recognized for receivables that are past due by a predefined period of time. Receivables from policyholders past due are valued at the average historical recovery rate. **Receivables from agents** are reduced by specific allowances and a general allowance in the amount of the likely default. The maturity of the receivables is less than one year.

Receivables from reinsurance business comprise amounts derived from both inward and outward reinsurance business. The balance of €46,740,155.11 as of December 31, 2017 arose for the most part from inward reinsurance business at the headquarters in Germany and at the branches in Spain, Italy, and the Netherlands. The amounts recognized are the outstanding balances. The breakdown by primary insurer or reinsurer was as follows:

Insurance companies

<i>(Balance in €'000)</i>	Dec. 31, 2017	Dec. 31, 2016
UNIPOL Assicurazioni, Italy, BBB- rating	23,367.1	23,791.4
ABN-AMRO Verzekeren, Netherlands, A+ rating	4,448.5	4,495.9
REALE, Spain and Italy, BBB+ rating	3,733.8	2,914.4
Noordhollandsche van 1816, Netherlands, no rating	3,215.5	3,129.3
GROUPAMA, Spain and Italy, BBB+ rating	2,005.3	0.0
Italiana Assicurazioni, Italy, BBB+ rating	947.3	669.3
Cattolica, Italy, BBB- rating	901.3	0.0
Intessa San Paolo, Italy, BBB+ rating	609.5	0.0
Helvetia, Italy, A rating	586.2	0.0
BRIT Syndicate 2987 at Lloyd's, United Kingdom, AA- rating	571.3	765.8
Sundry balances	6,354.4	9,070.2
	46,740.2	44,836.3

Miscellaneous receivables mainly comprise balances from intragroup services and items arising from the processing of leases, recourse claims (subrogation), payment receipts, accounts payable with a debit balance, and advances paid to employees. All items are due within one year. They are recognized at their nominal amounts.

In accordance with section 253 (1) sentence 1 HGB, **property and equipment** is recognized at cost and depreciated using the straight-line method over the standard operating useful life.

Inventories are determined by carrying out physical inventory checks. They are valued at cost and reduced by appropriate write-downs to account for storage risk and impaired marketability.

Bank balances, checks, and cash on hand are recognized at cost. This equates to the nominal amount. Bank balances denominated in foreign currency were translated using the middle spot exchange rate as of the reporting date, disregarding both historical cost convention and the realization principle. Balances are documented in the form of bank statements and cash records. Payment orders that had been issued but not executed as of the reporting date were deducted from the balances for the purposes of the carrying amounts reported on the balance sheet.

Other assets are recognized at their nominal amount, which equates to their cost. The residual maturities are less than one year.

Prepaid expenses and accrued income mainly consist of accrued rights to interest not yet due in the income period before the balance sheet date. As of December 31, 2017, this item also included premiums in connection with registered bonds amounting to €28,058.83 (December 31, 2016: €43,694.71).

If differences arise between the carrying amounts in the HGB financial statements and those in the tax base and these differences are expected to reverse in subsequent years, **deferred taxes** are recognized in respect of these differences using separate entity-specific tax rates applicable in the country in which the registered office of the entity concerned is situated. 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 of €6,080,380.79 were derecognized through the income statement in the year under review. The **subscribed capital** has been fully paid up by the shareholders. The **capital reserves** include amounts that shareholders have contributed to the equity of the Company without being granted preferences in accordance with section 272 (2) no. 4 HGB. The full amount of the statutory reserves has been recognized pursuant to section 150 (2) of the German Stock Corporation Act (AktG).

Subordinated liabilities have been issued by way of private placement to improve the own funds used to determine the solvency ratio. The registered bond with a value of €30,000.0 thousand has a fixed maturity of ten years and will be redeemed on July 29, 2024. The subordinated registered bond has been recognized at its settlement amount. These bonds were not, and are not, negotiable in Germany on a regulated market within the meaning of section 2 (5) of the German Securities Trading Act (WpHG).

Gross unearned premiums for direct insurance business are calculated pro rata temporis for each individual policy on the basis of the premiums and cancellations posted, less the installment surcharges. The calculated unearned premiums are reduced by the income components intended to cover the acquisition costs. An individually determined proportion (branches) or a flat rate of 85 percent (Group headquarters) of the commissions and other remuneration for agents is recognized as a non-transferable income component. The gross unearned premiums for inward reinsurance business are recognized in accordance with the information provided by the primary insurer. The reinsurers' share of the unearned premiums is determined in accordance with the contractual agreements.

The **provision for outstanding claims** in relation to direct insurance business is recognized separately by event year for claims reported in the financial year concerned and for claims that have occurred up to the balance sheet date but have not yet been reported. A provision for claim settlement expenses is also recognized. These provisions are valued in accordance with prudent business practice, taking into account the ongoing need to satisfy the obligations under insurance contracts. Valuation is based on values as of the balance sheet date. The provisions are not discounted. The results from the group-based and individual valuations are reviewed on a portfolio basis using actuarial methods.

In the reporting year, the settlements in direct business for all classes of insurance amounted to 2.8 percent of the initial reserve (2016: 4.6 percent).

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 the United Kingdom is determined on the basis of past experience and statistics produced by the Group's own claims settlement company. The proportions relating to outward reinsurance business are calculated in accordance with the stipulations in the reinsurance treaties. In the year under review, currency-related adjustments to the claims reserves were applied on the basis of exchange rates at the end of each quarter. The resulting exchange differences were recognized under other net income/expense.

The **equalization provision** for the direct insurance and inward reinsurance business is recognized and valued in accordance with section 341h HGB in conjunction with section 29 RechVersV. The calculation is carried out separately for the direct insurance business and for the inward reinsurance business, in each case broken down by class of insurance. The calculated equalization provision is allocated between the Group headquarters and the branches according to gross premiums earned in each class of insurance.

The **lapse provision** reported under miscellaneous technical provisions to cover the discontinuation or reduction of technical risk is recognized in the amount of the estimated requirement.

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 (2) sentence 2 HGB on the basis of the 2005G mortality tables published by Professor Klaus Heubeck. 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. A discount rate of 3.68 percent was applied for the valuation as of December 31, 2017 (December 31, 2016: 4.01 percent). As of December 31, 2017, the difference between the application of the ten-year average and the seven-year average (2.80 percent; December 31, 2016: 3.24 percent) caused a reduction in the provision for pensions and other post-employment benefits of €21,524,915.00 (31 December 2016: €17,583,468.00).

The following actuarial parameters were used to calculate the obligations: earliest possible age under the German Pension Age Reform Act (RVAGAnpG), annual increase in salaries of 2.5 percent, annual increase in pension benefits of 1.75 percent (for Spain, 2.5 percent). The level of staff turnover taken into account reflects the generally observable age-dependent average for the industry and has only a minor impact on the settlement value.

In accordance with section 246 (2) sentence 2 HGB, assets from reinsurance are offset against the defined benefit obligation. As of December 31, 2017, the fair value of these assets amounted to €995,277.00. The settlement value of the offset liabilities amounted to €995,277.00. In addition, securities with a fair value of €2,691,376.00 in accordance with section 253 (1) sentence 4 HGB were offset against the present value of the obligation. The valuation at fair value gave rise to an amount of €273,656.00 that was not allowed to be distributed as a dividend pursuant to section 268 (8) sentence 3 HGB. Neither the option under section 28 (1) of the Introductory Act to the German Commercial Code (EGHGB), which permits provisions for pensions and other post-employment benefits not to be recognized for legacy entitlements, nor the transitional provision under sec-

tion 67 (1) EGHGB has been exercised. The long period of low interest rates has led to a shortfall of €274,983.33 in pension funds used to cover pension commitments to employees. This shortfall has been determined in accordance with actuarial principles and reported as a pension obligation. **Provisions for taxes** are recognized in the anticipated settlement amount determined in accordance with prudent business practice.

Provisions for early retirement obligations are recognized for those persons with whom individual contractual agreements have been reached. The provisions are calculated using actuarial principles; as of the reporting date, the amounts were discounted to present value using a discount rate of 2.80 percent.

In 2017, 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 2.80 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 **sundry provisions** 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 2.80 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.

Interest income of €34,399.06 (2016: €14,201.56) and interest expenses of €4,701.25 (2016: €95,303.60) arose from the discounting of provisions with a maturity of more than one year. **Deposits received** are accounted for at the nominal value of the collateral received. They have a residual maturity of less than one year, as underlying reinsurance agreements are renewed annually.

Other liabilities are recognized at their settlement value. The residual maturity is less than one year.

The **liabilities from direct insurance business** and **liabilities from reinsurance business** are valued at their nominal amount. Liabilities denominated in foreign currency were translated using the middle spot exchange rate as of the reporting date, disregarding both the historical cost convention and the realization principle. All non-interest-bearing **liabilities** are valued at the higher of their nominal amount or settlement value. **Miscellaneous liabilities** are recognized at their settlement value.

The **deferred income and accrued expenses** item largely comprises as yet unbilled ancillary cost advances in connection with leased out real estate. As of December 31, 2017, it also included discounts on registered bonds amounting to €13,354.46 (December 31, 2016: €15,675.86). **Deferred tax liabilities** arise in connection with differences between the reported carrying amounts in the financial statements in accordance with HGB and those in the tax base, where these differences are expected to reverse in subsequent years resulting in a future tax expense overall. These liabilities are recognized on the balance sheet in the amount, within each jurisdiction, of any excess deferred tax liability after netting with deferred tax assets.

Currency translation

The cost of investments is calculated using the transaction exchange rate on the date of acquisition. The quoted market price or market value for foreign shares in affiliated companies and equity investments is determined by using an exchange rate achievable over the medium term; all other assets are valued at the lower of the exchange rate on the date of payment or the exchange rate on the balance sheet date. The sundry assets and liabilities with a residual maturity of up to one year are translated using the middle spot rate on the balance sheet date, disregarding the historical cost convention and the realization principle. Income and expenses are recognized using the transaction exchange rate on the date of the relevant inflow or outflow. In the year under review, currency translation gave rise to income of €1,769,852.43 (2016: €25,190.13) and expenses of €105,153.96 (2016: €138,796.44).

Fair value disclosures pursuant to section 54 RechVersV

Fair values of land, land rights and buildings, including buildings on third-party land

Valuation reports have been prepared internally and by third parties to determine these fair values. These reports satisfy the requirements of section 55 (3) RechVersV. Each year, new valuation reports are prepared or the existing reports are revised based on updated underlying data.

Fair values for investments in affiliated companies and equity investments

The shares and equity investments have generally been valued using the income capitalization approach. In the case of companies that predominantly perform services for the ARAG Group and in the case of intermediate holding companies, the pro-rata net asset value has been used as the fair value. Due to the need to expedite year-end closing procedures (Solvency II), figures as of the end of the third quarter of 2017 were used in some instances. For equity investments and shares acquired recently, the carrying amount was used as the fair value.

Fair values of miscellaneous investments

The fair values of line items B. III. 1. and 2. on the balance sheet correspond to their quoted market price or market value as of the balance sheet date. The fair values of securities that are not exchange-traded (registered bonds, promissory notes) are calculated on the basis of the swap curve. This involves determining the discount rate on the swap curve corresponding to the maturity of the security being valued. Any spreads resulting from the structure of the individual security (maturity, collateral, credit rating, etc.) are taken into account as appropriate.

The fair values are shown in the '**Changes in investments in 2017**' table.

III. Insurance Disclosures

(€'000)	Direct insurance business				
	Legal insurance	Emergency assistance insurance	Other (misc. financial losses)	Total 2017	Total 2016
Gross premiums written	614,879	48,637	9,736	673,252	633,818
Gross premiums earned	615,157	47,979	9,804	672,940	626,475
Net premiums earned	-	-	-	-	-
Claims incurred	332,538	26,813	158	359,510	320,729
of which payments for claims	304,744	24,986	1,280	331,011	325,520
Insurance business operating expenses	275,354	23,235	5,772	304,360	281,344
of which front-end fees	86,161	18,708	710	105,579	97,839
of which administrative expenses	189,193	4,527	5,061	198,781	183,504
Change in equalization provision	0	-377	-396	-772	-2,536
Miscellaneous underwriting income and expenses	1,804	0	0	1,804	1,459
Underwriting result	9,069	-2,446	3,479	10,102	23,325
Technical provisions:					
Unearned premiums	146,035	3,303	4,606	153,944	153,631
Provision for outstanding claims	904,398	8,073	1,970	914,441	885,942
Equalization provision and similar provisions	0	6,735	3,325	10,060	9,288
Miscellaneous technical provisions	690	0	0	690	882

Number of insurance policies with a term of at least one year

Direct insurance business	2017	2016
(No.)		
Germany	1,495,840	1,446,227
International	2,664,666	2,692,257
Total	4,160,506	4,138,484

	Inward reinsurance business				Outward reinsurance business		Total insurance business		
	Legal insurance	Emergency assistance insurance	Other (misc. financial losses)	Total 2017	Total 2016	2017	2016	2017	2016
	181,559	14,665	529	196,752	190,798	-	-	870,004	824,616
	181,373	14,373	557	196,303	192,806	-	-	869,243	819,281
	-	-	-	-	-	1,201	5,029	868,042	814,252
	90,410	15,474	-160	105,724	96,153	2,488	1,489	462,746	415,393
	77,743	15,068	55	92,866	83,818	1,704	856	422,172	408,482
	84,456	431	235	85,123	85,631	302	2,590	389,181	364,385
	472	363	5	839	1,052	-	-	-	-
	83,985	68	231	84,283	84,579	-	-	-	-
	-1,920	-127	-260	-2,307	-3,020	0	0	-3,079	-5,556
	0	0	0	0	0	0	0	1,804	1,459
	4,586	-1,659	222	3,150	8,002	-1,589	950	14,841	30,377
	41,249	5,305	131	46,686	46,618	1,418	1,417	199,212	198,832
	185,666	2,237	113	188,015	176,912	2,568	1,784	1,099,888	1,061,070
	6,282	127	405	6,813	4,506	0	0	16,873	13,794
	0	0	0	0	0	0	0	690	882

Source of insurance business by premiums written

Country/source	Direct insurance business			Inward reinsurance business			Total business
	Legal insurance	Emergency assistance insurance	Other (misc. financial losses)	Legal insurance	Emergency assistance insurance	Other (misc. financial losses)	
(€'000)							
Germany	349,202	0	0	0	0	0	349,202
Spain	51,716	48,349	5,039	19,078	14,665	193	139,040
Netherlands	92,531	0	0	49,929	0	0	142,460
Italy	28,808	0	4,697	89,678	0	336	123,519
Belgium	23,774	0	0	743	0	0	24,517
Austria	61,072	0	0	0	0	0	61,072
Slovenia	2,277	0	0	0	0	0	2,277
Greece	5,042	0	0	44	0	0	5,086
USA	0	0	0	285	0	0	285
UK	0	0	0	21,637	0	0	21,637
Portugal	455	288	0	165	0	0	908
Total	614,879	48,637	9,736	181,559	14,665	529	870,004

IV. Non-Insurance Disclosures

Changes in investments in 2017:

Changes in asset items A., B. I. to IV. from January 1 to December 31, 2017

Type of investment	Balance Jan. 1, 2017	Currency differences	Additions	Disposals
(€)				
A. Intangible assets				
1. Miscellaneous intangible assets	8,329,472.13	0.00	3,137,319.29	14,029.55
Total	8,329,472.13	0.00	3,137,319.29	14,029.55
B. I. Land, land rights and buildings, including buildings on third-party land	97,563,670.52	0.00	20,015.35	1,586,192.46
B. II. Investments in affiliated companies and equity investments				
1. Shares in affiliated companies	225,017,698.96	0.00	77,190,009.32	28,800,000.00
2. Lending to affiliated companies	1,655,527.11	0.00	0.00	1,655,527.11
3. Equity investments	16,887,569.37	0.00	0.00	0.00
Total investments in affiliated companies and equity investments	243,560,795.44	0.00	77,190,009.32	30,455,527.11
B. III. Miscellaneous investments				
1. Equities, investment fund shares/units, and other variable-yield securities	625,493,318.99	0.00	14,993,776.19	25,880,796.57
2. Bearer bonds and other fixed-income securities	301,550,383.27	0.00	130,698,634.42	33,695,122.88
3. Loans secured by mortgages or land charges and fixed-income receivables	3,975,000.00	0.00	5,504,927.98	300,000.00
4. Miscellaneous lending				
a) Registered bonds	140,511,291.88	0.00	0.00	0.00
b) Promissory notes and loans	243,995,110.85	0.00	18,000,000.00	10,035,248.41
c) Sundry lending	150,107.42	0.00	23,200.00	94,229.34
5. Bank deposits	98,570,813.32	0.00	50,000,000.00	90,601,847.32
6. Other investments	5,331,278.41	0.00	62,267.47	858,011.57
Total miscellaneous investments	1,419,577,304.14	0.00	219,282,806.06	161,465,256.09
B. IV. Deposits with ceding insurers	44,388,849.23	0.00	9,615,627.18	4,327,546.91
Total investments	1,805,090,619.33	0.00	306,108,457.91	197,834,522.57
Total including intangible assets	1,813,420,091.46	0.00	309,245,777.20	197,848,552.12

Land, land rights and buildings, including buildings on third-party land, with a carrying amount of €30,692,648.70 (December 31, 2016: €31,582,286.26) are used for the Company's own business operations.

Reversals of write-downs	Depreciation/ amortization	Write-downs	Balance Dec. 31, 2017	Cost/ nominal amount	Fair value as of Dec. 31, 2017	Hidden reserves
0.00	3,794,348.24	0.00	7,658,413.63	40,169,791.50	7,658,413.63	0.00
0.00	3,794,348.24	0.00	7,658,413.63	40,169,791.50	7,658,413.63	0.00
0.00	966,515.49	1,473,390.08	93,557,587.84	100,828,458.51	151,184,615.21	57,627,027.37
0.00	0.00	391,000.00	273,016,708.28	354,015,167.59	523,953,101.21	250,936,392.93
0.00	0.00	0.00	0.00	0.00	0.00	0.00
0.00	0.00	0.00	16,887,569.37	26,161,255.48	36,822,000.00	19,934,430.63
0.00	0.00	391,000.00	289,904,277.65	380,176,423.07	560,775,101.21	270,870,823.56
3,896,140.98	0.00	879,593.43	617,622,846.16	628,811,554.84	639,925,259.02	22,302,412.86
190,557.75	0.00	1,894,253.76	396,850,198.80	400,224,756.89	418,522,864.97	21,672,666.17
0.00	0.00	0.00	9,179,927.98	9,179,927.98	9,179,927.98	0.00
0.00	0.00	0.00	140,511,291.88	140,511,291.88	146,166,178.38	5,654,886.50
0.00	0.00	0.00	251,959,862.44	251,959,817.91	267,849,631.72	15,889,769.28
0.00	0.00	0.00	79,078.08	79,078.08	79,078.08	0.00
0.00	0.00	0.00	57,968,966.00	57,968,966.00	57,968,966.00	0.00
0.00	0.00	0.00	4,535,534.31	4,535,534.31	7,452,962.91	2,917,428.60
4,086,698.73	0.00	2,773,847.19	1,478,707,705.65	1,493,270,927.89	1,547,144,869.06	68,437,163.41
0.00	0.00	0.00	49,676,929.50	49,676,929.50	49,676,929.50	0.00
4,086,698.73	966,515.49	4,638,237.27	1,911,846,500.64	2,023,952,738.97	2,308,781,514.98	396,935,014.34
4,086,698.73	4,760,863.73	4,638,237.27	1,919,504,914.27	2,064,122,530.47	2,316,439,928.61	396,935,014.34

In addition, there is an equity investment in a property-managing entity in the form of a partnership under the German Civil Code (GbR). The sole purpose of this entity is to operate an administrative building. The equity investment is reported under land and buildings. As of December 31, 2017, the carrying amount of the equity investment was €39,593,856.28 (December 31, 2016: €41,000,564.40). Some 98.0 percent (December 31, 2016: 97.9 percent) of the property managed by the entity (headquarters of the ARAG Group in Düsseldorf) is used for the Company's own business operations. The remaining proportion is used by affiliated companies for their operations.

Investment fund disclosures

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

Institutional funds

Institutional fund	Type of fund	Investment objective	Carrying amount as of Dec. 31, 2017	Market value as of Dec. 31, 2017	Difference	Dividend in 2017	Redemption
			(€)	(€)	(€)	(€)	
ADRENT	Fixed-income fund	Increased income	51,269,359.25	53,448,827.56	2,179,468.31	1,149,228.73	At any time
ATRI	Fixed-income fund	Increased income	151,654,738.13	151,182,469.40	-472,268.73	3,363,584.94	At any time
ARRE	Mixed fund	Increased income	252,714,620.12	266,843,617.07	14,128,996.95	6,730,573.50	At any time
ARI 1	Fixed-income fund	Increased income	71,016,870.03	71,035,471.52	18,601.49	3,534,527.76	At any time
AAF	Equity fund	Increased income	21,936,721.59	24,089,311.51	2,152,589.92	580,245.03	At any time
EMA	Equity fund	Increased income	27,095,680.80	27,928,479.38	832,798.58	509,650.48	At any time
SIVE Fonds							
INKA	Equity fund	Increased income	24,160,914.28	26,098,534.56	1,937,620.28	2,858,475.66	At any time
			599,848,904.20	620,626,711.00	20,777,806.80	18,726,286.10	

The investment objectives of the funds – which can be traded on any stock market trading day – are based on the relevant benchmarks derived from the strategic investment structure.

The breakdown of the **other assets** is as follows:

Other assets

(€)	Dec. 31, 2017	Dec. 31, 2016
Income tax refund claim under current income tax assessment and on the basis of tax audit findings	17,809,404.54	27,765,955.71
Claims for interest not yet due on tax refunds	2,365,322.02	2,940,661.64
Italian insurance tax refund claim	1,972,652.92	2,020,847.63
Italian income tax refund claim	926,841.17	371,656.84
Spanish income tax refund claim	0.00	420,420.73
Claim under section 37 (5) of the German Corporation Tax Act (KStG)	0.00	4,608,798.81
Sundry items	216,362.52	0.00
Total	23,290,583.17	38,128,341.36

Deferred taxes disclosures

Deferred tax liabilities arising in connection with carrying amounts of balance sheet items that are only permissible for tax purposes have been netted with deferred tax assets arising on differences between carrying amounts in the HGB financial statements and those in the tax base. Any excess deferred tax assets after netting are not reported.

Change in deferred taxes

Balance sheet item (€'000)	Jan 1, 2017	Change in 2017	Dec 31, 2017
Intangible assets	1,349	432	1,781
Investments	371	-3,864	-3,493
Receivables	6,903	-1,235	5,668
Miscellaneous assets	1,934	75	2,009
Prepaid expenses and accrued income	0	0	0
Technical provisions	54,250	18,706	72,956
Other provisions	44,869	10,222	55,091
Other liabilities	-54	54	0
Deferred income and accrued expenses	0	0	0
Off-balance-sheet additions	-1,697	1,697	0
Assessment basis from tax group members (see below)			
- ARAG Allgemeine Versicherungs-AG	57,328	-5,162	52,166
- Interlloyd Versicherungs-AG	4,273	-97	4,176
Assessment basis for deferred taxes	169,526	20,829	190,355
Deferred taxes	49,878	4,818	54,696
Reductions in 2016 and 2017	-43,798	-10,898	-54,696
Recognized deferred tax assets	6,080	-6,080	0

Assessment basis from tax group members

(€'000)	Jan 1, 2017	Change in 2017	Dec 31, 2017
Investments	3,105	-229	2,876
Miscellaneous assets	322	-344	-22
Technical provisions	50,065	-5,887	44,178
Other provisions	8,109	1,201	9,310
Assessment basis for deferred taxes	61,601	-5,259	56,342

Deferred taxes are calculated using the current income tax rate of the country that will have the right to levy tax on the assessment basis concerned at the time that the differences reverse in accordance with the relevant double taxation convention. For financial reporting purposes, the effects of the reversal of the differences between the HGB financial statements and the tax base are reviewed in terms of their impact on the basis of tax assessment. The recognized deferred tax liabilities of €10,534.17 resulted from excess liabilities in Austria.

Disclosures on amounts prohibited from being distributed as a dividend

Overall, the following amounts are not allowed to be paid out as a dividend pursuant to section 268 (8) HGB:

Amounts prohibited from being distributed

(€)	Dec. 31, 2017	Dec. 31, 2016
Difference pursuant to section 253 (6) sentence 1 HGB (provision for pensions and other post-employment benefits)	21,524,915.00	17,583,468.00
Amount by which the carrying amount of assets exceeds the cost (plan assets – valued at fair value – covering personnel liabilities)	273,656.00	403,818.70
Net asset balance of deferred tax assets and deferred tax liabilities	0.00	6,080,380.79
Total amount prohibited from being distributed	21,798,571.00	24,067,667.49

The amount is covered in full by freely available equity components.

Equity

(€)		Dec. 31, 2017
Total		439,404,753.50
I. Subscribed capital		
The share capital amounts to		100,000,000.00
<p>The share capital is divided into 62,500 no-par-value registered shares. All the shares are fully paid up. AFI Verwaltungs-Gesellschaft mbH, Düsseldorf, and ARAG Holding SE, Düsseldorf, each own more than one quarter of the shares in the Company. ARAG Holding SE indirectly owns the majority of the shares in the Company.</p>		
II. Capital reserves in accordance with section 272 (2) no. 4 HGB		
Brought forward as of January 1, 2017	81,772,569.19	
Changes in the reporting year	0.00	
Balance as of December 31, 2017		81,772,569.19
III. Revenue reserves		
1. Statutory reserves		
Brought forward as of January 1, 2017	10,000,000.00	
Appropriation from profit	0.00	
Balance as of December 31, 2017		10,000,000.00
<p>The full amount of the reserve has been recognized pursuant to section 150 (2) of the German Stock Corporation Act (AktG).</p>		
2. Other revenue reserves		
Brought forward as of January 1, 2017	198,900,000.00	
Additions approved by the Annual General Meeting	16,700,000.00	
Appropriation from profit	0.00	
Balance as of December 31, 2017		215,600,000.00
		225,600,000.00
IV. Net retained profit		
Net retained profit as of December 31, 2016		31,701,021.52
Appropriation of profits: dividend		- 15,000,000.00
Appropriation of profits: appropriation to other revenue reserves		- 16,700,000.00
Net income for 2017		32,031,162.79
Appropriation to statutory reserves (section 150 (2) AktG)		0.00
Appropriation to other revenue reserves		0.00
Net retained profit as of December 31, 2017		32,032,184.31

Provisions for pensions and other post-employment benefits

Since 2010, this item has also included the offsetting of pension benefit entitlements under reinsurance in accordance with section 246 (2) sentence 2 HGB. The breakdown of the item as of December 31, 2017 was therefore as follows:

Defined benefit obligations

(€)	Dec. 31, 2017	Dec. 31, 2016
Amount required to settle the vested entitlements	175,957,362	169,353,823
of which offsetable against pension insurance assets	-995,277	-1,215,595
of which offsetable against securities	-2,691,376	-3,823,439
Remaining amount	172,270,709	164,314,789

The transitional provision under section 67 (1) EGHGB and the option under section 28 (1) EGHGB have not been exercised. The defined benefit obligations have been recognized in full.

Miscellaneous provisions

(€)	Dec. 31, 2017	Dec. 31, 2016
Outstanding employee remuneration	14,515,858.34	15,057,251.24
Outstanding commission payments	12,195,448.58	12,406,603.06
Provision for outstanding invoices	7,848,658.17	12,255,347.55
Early retirement and pre-retirement part-time working obligations	5,612,789.31	3,326,544.25
Long-service provision	3,465,038.60	3,265,485.21
Severance payments (Austria and Slovenia)	2,600,071.19	2,641,980.73
Interest on taxes and additional tax-related charges	2,506,434.00	3,068,358.00
Compensation claims for agents leaving the Company	2,440,136.18	2,533,660.36
Performance-related and business-plan remuneration for agents	1,929,000.00	1,406,000.00
Costs for financial statements and tax audit	1,884,620.00	1,482,773.59
Severance payments	1,047,190.08	128,700.00
Sales competition awards	829,367.00	888,400.00
Supervisory Board and Advisory Council remuneration	586,368.00	589,406.50
Redundancy scheme and restructuring obligations	578,771.26	34,720.78
Current litigation costs	442,902.59	955,590.38
Subsequent performance obligations related to services	0.00	1,672,064.00
Sundry other provisions	4,588,635.78	3,494,807.26
Total	63,071,289.08	65,207,692.91

Prepaid expenses and accrued income, deferred income and accrued expenses

Prepaid expenses and accrued income includes premiums of €28,058.83 (December 31, 2016: €43,694.71), and deferred income and accrued expenses discounts of €13,354.46 (December 31, 2016: €15,675.86) pursuant to section 341 c (2) HGB. These amounts are reclassified to income over the maturity of the investments concerned.

Net extraordinary income/expense

No extraordinary income or expenses arose in the year under review.

Tax expense

The income taxes reported in the income statement included the following: €16,983,709.30 (2016: €11,845,606.16) related to the year under review and income of €1,186,339.67 (2016: income of €345,991.03) related to prior years. They also included expenses arising from the change in the balance of deferred taxes amounting to €6,090,914.96 (2016: €23,655,894.04) and expenses for foreign taxes not attributable to permanent establishments in the amount of €293,322.73 (2016: €1,000.00).

V. Report on Post-Balance Sheet Events

There were no events of particular significance after December 31, 2017.

VI. Other Disclosures

Commissions and other remuneration for insurance agents, staff costs

(€)	2017	2016
1. Commissions of all types for insurance agents within the meaning of section 92 HGB for direct insurance business	164,633,485.57	171,423,221.79
2. Other remuneration for insurance agents within the meaning of section 92 HGB	14,741,441.86	13,233,404.15
3. Wages and salaries	158,086,982.44	148,481,534.81
4. Social security and other employee benefit expenses	27,672,471.24	26,138,716.31
5. Pension and other post-employment benefit expenses	20,758,457.59	5,395,715.58
6. Total expenses	385,892,838.70	364,672,592.64

Contingent liabilities and miscellaneous financial commitments (section 251 and section 285 HGB)

There were no known **miscellaneous financial commitments** arising outside the insurance business that were significant to the assessment of the Company's financial position. ARAG SE is a partner in ARAG 2000 Grundstücksgesellschaft bürgerlichen Rechts and is jointly and severally liable for the obligations of this partnership without limitation on the basis of its entire assets.

There are **unpaid contributions** in respect of the following entities:

Unpaid contributions/obligations to pay in capital

(€)	
ARAG IT GmbH, Düsseldorf	1,495,000.00
ARAG Legal Services B.V., Leusden, Netherlands	6,977,311.00
Foyer-ARAG S.A., Leudelange, Luxembourg	24,788.00
RREEF Pan-European Infrastructure Feeder GmbH & Co. KG	233,525.74
ACF V Growth Buy-out Europe GmbH & Co. KG	451,942.92
AXA LBO Fund V Core	46,256.00
AXA LBO Fund V Supplementary	29,960.00

None of the unpaid contributions have been called up. It would be reasonable to expect contributions to be called up by RREEF Pan-European Infrastructure Feeder GmbH & Co. KG, ACF V Growth Buy-out Europe GmbH & Co. KG, and AXA LBO Fund V in the near future. The sundry unpaid contributions will not be called up for the time being. Investment agreements with a total volume of €54,342,467.03 have been concluded through the affiliated company ALIN 1 GmbH & Co. KG with various private equity funds. Calls from the funds result in cash being paid into ALIN 1 GmbH & Co. KG shortly before payment is due in order to provide the required liquidity. Taking account of the liquidity remaining in the company, calls at short notice of €39,285,889.63 are expected on the basis of the open-ended investment agreements.

Auditor's fees

The Company's Supervisory Board agreed fees with the auditors for the audit of the 2017 annual financial statements and Solvency II balance sheet as of December 31, 2017. A provision of €514,100.00 was recognized as an expense in the income statement for audit services, including out-of-pocket expenses and non-deductible VAT. Fees of €58,573.29 incurred for services provided by the auditors in connection with compliance management were also recognized in the income statement under other attestation services. Expenses of €187,337.97 were incurred in relation to tax consultancy services. These services mainly comprised the provision of support for restructuring in the Group and the processing of current tax matters. Expenses for miscellaneous services amounted to €73,436.12 and primarily related to the provision of project-related consultancy. As there was no entitlement to offset input VAT, the VAT was included in the recognized expense. The auditors also provided services for subsidiaries in connection with voluntary audits of annual financial statements and as an independent trustee in the motor insurance business.

Employees

ARAG SE employed an average of 2,631 (2016: 2,494) people in 2017. As of December 31, 2017, the Company had 2,632 (December 31, 2016: 2,564) employees.

Workforce breakdown

Unit	As of December 31, 2017	As of December 31, 2016
Central Group Functions	80	80
Accounting, Asset Management, Taxes, Central Services	178	184
Sales, Products and Innovation	341	229
Customer and Claims Service, IT Steering	420	406
Product Development/Innovation	0	75
Risk Management/Controlling	39	44
Group Development, Business Organization	18	19
Netherlands Branch	583	594
Belgium Branch	72	76
Italy Branch	138	141
Spain Branch	475	422
Portugal Branch	7	7
Austria Branch	111	99
Slovenia Branch	11	11
Greece Branch	22	23
Non-active employees (works council, parental leave, pre-retirement part-time employment)	137	154
Total	2,632	2,564
Plus: trainees	6	5
Plus: interns and volunteers	3	1

Supervisory Board, Advisory Council, and Management Board remuneration pursuant to section 285 no. 9 a HGB

The expense for Supervisory Board remuneration amounted to €499,800.00 and for the Advisory Council €86,568.00. The Management Board's remuneration came to €6,100,486.30, with that for the former members of the Management Board and their surviving dependants totaling €1,945,930.63. A provision of €28,281,946.00 was recognized for current pensions and vested pension entitlements of former members of the Management Board and their surviving dependants.

The members of the Supervisory Board, Advisory Council, and Management Board are listed on pages 90 to 92 of this report.

Group affiliation

The Company and its subsidiaries were included in the consolidated financial statements of ARAG Holding SE for the period ended December 31, 2017. The consolidated financial statements of ARAG Holding SE are published in the electronic Federal Gazette and in the company register of the German Federal Ministry of Justice and Consumer Protection. The Company does not prepare its own consolidated financial statements, as the consolidated financial statements of ARAG Holding SE have an exempting effect pursuant to section 291 HGB.

VII. Proposed Appropriation of Profit

The breakdown of net retained profit is as follows:

Net retained profit

(€)	
Net income for the year	32,031,162.79
Appropriation to other revenue reserves	0.00
Profit brought forward from 2016	1,021.52
Net retained profit	32,032,184.31

It is proposed that this net retained profit be used to pay a dividend of €20,000,000.00 to the shareholders. An amount of €12,000,000.00 is to be appropriated to other revenue reserves. The remaining sum of €32,184.31 is carried forward to the next period.

Düsseldorf, March 13, 2018

ARAG SE

The Management Board

Dr. Dr. h. c. Paul-Otto Faßbender

Dr. Renko Dirksen

Dr. Matthias Maslaton

Werner Nicoll

Hanno Petersen

Dr. Joerg Schwarze

Independent Auditor's Report*

To ARAG SE, Düsseldorf

Report on the Audit of the Annual Financial Statements and of the Management Report

Audit Opinions

We have audited the annual financial statements of ARAG SE, Düsseldorf, which comprise the balance sheet as at December 31, 2017, and the statement of profit and loss for the financial year from January 1 to December 31, 2017, and notes to the financial statements, including the recognition and measurement policies presented therein. In addition, we have audited the management report of ARAG SE for the financial year from January 1 to December 31, 2017. We have not audited the content of the statement on corporate governance pursuant to § [Article] 289 f Abs. [paragraph] 4 HGB [Handelsgesetzbuch: German Commercial Code] (disclosures on the proportion of women) in accordance with the German legal requirements.

In our opinion, on the basis of the knowledge obtained in the audit,

- the accompanying annual financial statements comply, in all material respects, with the requirements of German commercial law and give a true and fair view of the assets, liabilities and financial position of the Company as at December 31, 2017 and of its financial performance for the financial year from January 1 to December 31, 2017 in compliance with German Legally Required Accounting Principles, and
- the accompanying management report as a whole provides an appropriate view of the Company's position. In all material respects, this management report is consistent with the annual financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our audit opinion on the management report does not cover the content of the statement on corporate governance referred to above.

Pursuant to § 322 Abs. 3 Satz [sentence] 1 HGB, we declare that our audit has not led to any reservations relating to the legal compliance of the annual financial statements and of the management report.

* 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 single-entity financial statements, is authoritative.

Basis for the Audit Opinions

We conducted our audit of the annual financial statements and of the management report in accordance with §317 HGB and the EU Audit Regulation (No. 537/2014, referred to subsequently as "EU Audit Regulation") and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Our responsibilities under those requirements and principles are further described in the "Auditor's Responsibilities for the Audit of the Annual Financial Statements and of the Management Report" section of our auditor's report. We are independent of the Company in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements.

In addition, in accordance with Article 10 (2) point (f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the annual financial statements and on the management report.

Key Audit Matters in the Audit of the Annual Financial Statements

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the annual financial statements for the financial year from January 1 to December 31, 2017. These matters were addressed in the context of our audit of the annual financial statements as a whole, and in forming our audit opinion thereon; we do not provide a separate audit opinion on these matters.

In our view, the matters of most significance in our audit were as follows:

1. Measurement of investments
2. Measurement of claims provisions

Our presentation of these key audit matters has been structured in each case as follows:

1. Matter and issue
2. Audit approach and findings
3. Reference to further information

Hereinafter We Present the Key Audit Matters:**1. Measurement of Investments**

1. In the Company's annual financial statements investments amounting to EUR 1,912 million (89.9% of total assets) are reported in the balance sheet. Investments that are not measured on the basis of stock exchange prices or other market prices (e.g. unquoted equity investments as well as other illiquid bonds) are associated with increased risk regarding measurement due to the necessity of using model-based calculations. The executive directors are required to exercise judgment and make estimates and assumptions in this context. Minor changes to those assumptions or to the methods used may have a material impact on the measurement of investments. Due to the material significance of the amounts of investments for the assets liabilities and financial performance of the Company as well as the considerable scope for judgment on the part of the executive directors and the associated uncertainties in the estimations made, the measurement of investments was of particular significance in the context of our audit.
2. Given the significance of investments for the Company's overall business, as part of our audit we assessed the assumptions made by the executive directors and the models used by the Company together with our internal specialists for investments. Thereby, we based our assessment on our industry expertise and experience, among other things, and considered recognized market practices. In addition, we evaluated the design and effectiveness of the controls established by the Company for the purpose of measuring investments and recording the earnings from investments. On that basis, we carried out additional analytical audit procedures and tests of details relating to the measurement of investments. Among other things, we also examined the underlying amounts recorded and their recoverability on the basis of the documentation made available, and we evaluated the consistent application of the measurement methods and the allocation of amounts to the correct periods. Furthermore, we assessed the valuation reports prepared respectively obtained by the Company (including the measurement parameters used and the assumptions made) for its material equity investments. Based on our audit procedures, we were able to satisfy ourselves that the estimates and assumptions made by the executive directors for the purpose of measuring the investments are substantiated and sufficiently documented.
3. The Company's disclosures on the measurement of investments are contained in section II "Disclosures on Accounting Policies" of the notes to the financial statements.

2. Measurement of Claims Provisions

1. In the annual financial statements of the Company technical provisions (“claims provisions”) amounting to EUR 1,100.0 million (51.7% of total assets) are reported under the “Provisions for unsettled claims” balance sheet item. The methods used to determine the amount of the claims provisions and the calculation parameters are based on judgments and assumptions made by the executive directors. Minor changes to those assumptions or to the methods used may have a material impact on the measurement of the claims provisions. Due to the material significance of the amounts of these provisions for the assets, liabilities and financial performance of the Company as well as the considerable scope for judgment on the part of the executive directors and the associated uncertainties in the estimations made, the measurement of the claims provisions was of particular significance in the context of our audit.
2. Given the significance of the claims provisions for the Company’s overall business, as part of our audit we assessed the assumptions made by the executive directors and the methods used by the Company together with our internal measurement specialists. Thereby, we based our assessment on our industry expertise and experience, among other things, and considered recognized methods. We also evaluated the design and effectiveness of the controls established by the Company for the purpose of calculating and recording claims provisions. On that basis, we carried out additional analytical audit procedures and tests of details relating to the measurement of the claims provisions. Among other things, we also reconciled the data on which the calculation of the settlement amount was based with the underlying documentation. Therewith, we assessed the results of the Company’s calculations of the amount of the provisions with reference to the applicable legal requirements and evaluated the consistent application of the measurement methods and the allocation of amounts to the correct periods. Based on our audit procedures, we were able to satisfy ourselves that the estimates and assumptions made by the executive directors for the purpose of measuring the claims provisions are substantiated and sufficiently documented.
3. The Company’s disclosures on the measurement of claims provisions are contained in section II “Disclosures on Accounting Policies” of the notes to the financial statements.

Other Information

The executive directors are responsible for the other information. The other information comprises the statement on corporate governance pursuant to §289f Abs. 4 HGB (disclosures on the proportion of women).

The other information comprises further the remaining parts of the annual report – excluding cross-references to external information – with the exception of the audited annual financial statements, the audited management report and our auditor's report.

Our audit opinions on the annual financial statements and on the management report do not cover the other information, and consequently we do not express an audit opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in so doing, to consider whether the other information

- is materially inconsistent with the annual financial statements, with the management report or our knowledge obtained in the audit, or
- otherwise appears to be materially misstated.

Responsibilities of the Executive Directors and the Supervisory Board for the Annual Financial Statements and the Management Report

The executive directors are responsible for the preparation of the annual financial statements that comply, in all material respects, with the requirements of German commercial law, and that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Company in compliance with German Legally Required Accounting Principles. In addition, the executive directors are responsible for such internal control as they, in accordance with German Legally Required Accounting Principles, have determined necessary to enable the preparation of annual financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the annual financial statements, the executive directors are responsible for assessing the Company's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting, provided no actual or legal circumstances conflict therewith.

Furthermore, the executive directors are responsible for the preparation of the management report that as a whole provides an appropriate view of the Company's position and is, in all material respects, consistent with the annual financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In addition, the executive directors are responsible for such

arrangements and measures (systems) as they have considered necessary to enable the preparation of a management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the management report.

The supervisory board is responsible for overseeing the Company's financial reporting process for the preparation of the annual financial statements and of the management report.

Auditor's Responsibilities for the Audit of the Annual Financial Statements and of the Management Report

Our objectives are to obtain reasonable assurance about whether the annual financial statements as a whole are free from material misstatement, whether due to fraud or error, and whether the management report as a whole provides an appropriate view of the Company's position and, in all material respects, is consistent with the annual financial statements and the knowledge obtained in the audit, complies with the German legal requirements and appropriately presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our audit opinions on the annual financial statements and on the management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with §317 HGB and the EU Audit Regulation and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW) will always detect a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these annual financial statements and this management report.

We exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the annual financial statements and of the management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our audit opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.
- Obtain an understanding of internal control relevant to the audit of the annual financial statements and of arrangements and measures (systems) relevant to the audit of the management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an audit opinion on the effectiveness of these systems of the Company.

- Evaluate the appropriateness of accounting policies used by the executive directors and the reasonableness of estimates made by the executive directors and related disclosures.
- Conclude on the appropriateness of the executive directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the annual financial statements and in the management report or, if such disclosures are inadequate, to modify our respective audit opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to be able to continue as a going concern.
- Evaluate the overall presentation, structure and content of the annual financial statements, including the disclosures, and whether the annual financial statements present the underlying transactions and events in a manner that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Company in compliance with German Legally Required Accounting Principles.
- Evaluate the consistency of the management report with the annual financial statements, its conformity with German law, and the view of the Company's position it provides.
- Perform audit procedures on the prospective information presented by the executive directors in the management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by the executive directors as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate audit opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, the related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the annual financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

Other Legal and Regulatory Requirements

Further Information Pursuant to Article 10 of the EU Audit Regulation

We were elected as auditor by the supervisory board on April 28, 2017. We were engaged by the supervisory board on October 17, 2017. We have been the auditor of ARAG SE, Düsseldorf, without interruption since the financial year 1992.

We declare that the audit opinions expressed in this auditor's report are consistent with the additional report to the audit committee pursuant to Article 11 of the EU Audit Regulation (long-form audit report).

German Public Auditor Responsible for the Engagement

The German Public Auditor responsible for the engagement is Ludger Koslowski.

Düsseldorf, March 16, 2018

PricewaterhouseCoopers
Gesellschaft mit beschränkter Haftung
Wirtschaftsprüfungsgesellschaft

Ludger Koslowski Wirtschaftsprüfer (German Public Auditor)	Sven Capousek Wirtschaftsprüfer (German Public Auditor)
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Report of the Supervisory Board

In the year under review, the Supervisory Board carried out the tasks required of it by law, the articles of incorporation, and rules of procedure and continually monitored and advised the Management Board with regard to its running of the Company. The Supervisory Board was directly involved in all decisions of fundamental importance to the Company. The Management Board provided the Supervisory Board with regular, timely, and comprehensive written and oral reports on the economic situation and the performance of the Company and its subsidiaries, planned business policy, corporate planning, the risk situation, risk management, and significant individual transactions. The Management Board explained variances between the actual course of business and plans and targets individually, and these were noted by the Supervisory Board. Where management action required the approval of the Supervisory Board by law or other regulations, the Supervisory Board received detailed written information on the matter from the Management Board. The Supervisory Board discussed these reports extensively at its meetings, deliberated on them with the Management Board, and made the necessary decisions.

Last year, the full Supervisory Board held four ordinary meetings, at which it was able to satisfy itself that the Management Board was running the Company properly and appropriately. The Supervisory Board also met once for the constitutive meeting of the Supervisory Board and its committees. Outside the meetings, the chairman of the Supervisory Board was also in regular contact with the Management Board and was kept informed about the current business situation and major business transactions.

In 2017, the meetings of the Supervisory Board focused primarily on discussing medium- to long-term cost management in response to the disposal of the life insurance business and the advancing process of digitalization in the industry. The Supervisory Board also addressed the issue of succession planning as a result of a redistribution of responsibilities within the Management Board. In this regard, the Supervisory Board received detailed reports on special topics related to the newly created 'Products, Innovation and Sales' area of Management Board responsibility. A joint conference was held to enable the Supervisory Board to obtain in-depth information on the regulatory changes and requirements arising from the Solvency II Directive. In other discussions, the Supervisory Board covered the options for expanding the casualty and property insurance business in Italy, the quarterly results under HGB and Solvency II, and the projections for 2017. In addition, it received reports on the business performance of the Company and its affiliated companies. The Group risk strategy, the risk and controlling report, and the strategic planning for the next three years formed part of these reports.

Further matters addressed by the Supervisory Board included the appropriateness of Management Board remuneration and of the remuneration system used for employees. In this regard, it reached decisions to reorganize pension entitlements and variable remuneration for the Management Board and increase the sum insured in the directors' and officers' insurance policy (D&O insurance) taken out for the Management Board. A similar increase in D&O insurance for the Supervisory Board was proposed to the Annual General Meeting (AGM), where it was approved. The Supervisory Board agreed the introduction of

a digital meetings folder and digitalization of the board's activities; it decided on the necessary changes to statutes and proposed amendments to the articles of incorporation to the AGM, which the AGM then approved.

The full Supervisory Board proposed to the AGM that the Supervisory Board be reappointed without any changes. The AGM approved this proposal.

The Supervisory Board received regular reports on the progress of projects aimed at implementing the EU's Insurance Distribution Directive and General Data Protection Regulation, and consented to the creation of an audit committee in connection with the new EU Audit Regulation. As the new committee has the same members as the existing accounting committee already known at ARAG as the 'Audit Committee', the existing committee has been renamed 'Accounting and Audit Committee'.

The full Supervisory Board also discussed and redefined the strategic principles for underwriting new business.

Last but not least, the Supervisory Board addressed the issue of the gender composition of management in accordance with statutory requirements and specified new gender ratios for both the Management Board and the Supervisory Board.

The Supervisory Board did not make any decisions using written procedures.

The Supervisory Board has created three committees.

The Finance Committee held a total of seven meetings in 2017, including four ordinary meetings. Agenda items at meetings included the real estate report for all ARAG entities, ARAG's total exposure in respect of various banks, and the opportunities and risks from hidden reserves. In accordance with its responsibilities, it approved a number of capital additions, IT consultancy engagements for the coming year, and necessary appointments to governing bodies in subsidiaries. The Finance Committee also received reports on ARAG's IT security strategy and approved the rollout of new IT applications, both for the Group and for the Company. Reports were submitted to the committee at regular intervals on the performance of the newly established 'Justix' legaltech unit; there was also a presentation on purchasing management. The Finance Committee addressed the options for expanding the casualty and property insurance business in Italy and in this context made a decision to establish an Italian insurance brokerage agency.

With a view to developing further business lines, it was decided to restructure ARAG's operations in Norway, enabling (legal) services to also be provided to non-insurance customers in Scandinavia going forward.

Finally, a number of meetings of the Finance Committee addressed the acquisition of legal insurance portfolios currently available for sale and the general mergers and acquisitions strategy. In addition to meetings, the Finance Committee used a written procedure on a number of occasions to consent to the engagement of IT consultants, agree to a private equity investment, approve a settlement agreement between ARAG SE and ARAG Lebensversicherungs-AG, and agree to the sale of a property as well as other capital additions and HR decisions in accordance with its remit.

The Accounting and Audit Committee met on four occasions in the year under review. Besides the quarterly financial statements under HGB and Solvency II and forecasts for the 2017 annual financial statements, the committee discussed the strategic planning for the years 2018 to 2020 and recommended the plans to the Supervisory Board for approval. The Accounting and Audit Committee received a presentation on, and

approved, the 'Guidelines on reviewing and approving the legitimacy of the performance of non-audit services' and subsequently decided on the list of duties and responsibilities of the Accounting and Audit Committee. It also approved the list of non-audit services that the independent auditors would be permitted to provide. Finally, it discussed medium- to long-term cost management in response to the disposal of the life insurance business and the advancing process of digitalization in the industry.

The Accounting and Audit Committee did not make any decisions using written procedures.

The Human Resources Committee held four ordinary meetings in 2017. One resolution was also adopted using a written procedure. Topics discussed in the meetings included target agreements, the pension scheme and provision for surviving dependants, and the appropriateness of the Management Board's remuneration. A reorganization of variable remuneration for the Management Board was also addressed in this context. The committee carried out the annual review and acceptance of the 'fit and proper' guidance and remuneration policy, and issued the approvals pursuant to section 114 AktG in accordance with its responsibilities as specified in the rules of procedure.

In addition, the Human Resources Committee addressed the remuneration system, especially the new HR auditing obligations in accordance with statutory requirements. Another focus of discussions was ensuring compliance with the 'fit and proper' requirements under VAG and possible implications of a revocation by BaFin. The committee also discussed the requirement to adjust the sum insured under the D&O insurance policy and received reports on the pension arrangements in the international units.

Matters decided by means of a written procedure included the consents pursuant to section 114 AktG, responsibility for which is assigned to the Human Resources Committee in the rules of procedure.

Detailed reports on the committees' meetings and work were delivered at the Supervisory Board meetings.

The financial statements, which were prepared by the Management Board in accordance with the commercial-law accounting regulations for insurance companies, and the management report for 2017 were, together with the bookkeeping system, audited by PwC PricewaterhouseCoopers GmbH, Wirtschaftsprüfungsgesellschaft, Düsseldorf, which had been selected and engaged by the Supervisory Board on April 28, 2017 to carry out the audit and which issued an unqualified opinion.

All the members of the Accounting and Audit Committee of the Supervisory Board received the aforementioned documents, the annual report, the proposal for the appropriation of profit, and the auditor's report in good time before the Supervisory Board meeting on April 26, 2018. At the meeting, the Management Board also provided additional oral explanations of the documents. The auditors who had signed the auditor's report participated in the discussion of the documents by the Supervisory Board and the Accounting and Audit Committee, reported on the key findings of the audit, and were available to provide additional information.

The Accounting and Audit Committee had discussed these documents in detail prior to the meeting of the Supervisory Board and had recommended to the Supervisory Board that the financial statements and the management report be approved.

The Supervisory Board reviewed the financial statements, management report, and proposal for the appropriation of profit. There were no objections to be raised on the basis of the concluding findings of its review. Having carried out its own review and having taken into account the report of the Accounting and Audit Committee, the Supervisory Board agreed with the findings of the audit of the financial statements and management report by the auditors. The Supervisory Board approved the financial statements and management report and thereby adopted them. It also agreed with the Management Board's proposed appropriation of profit. The Supervisory Board proposes to the AGM that it formally approve the acts of the Management Board members.

The report to be submitted by the Management Board pursuant to section 312 AktG concerning relationships with affiliated companies was also reviewed. The review encompassed the completeness and accuracy of the details in the report on the basis of the right to inspect the books and papers of the Company and on the basis of the reports and information submitted by the Management Board. The review did not give rise to any objections.

The independent auditors also audited the report submitted by the Management Board pursuant to section 312 AktG and issued the following audit opinion:

"Following our audit and evaluation exercising all due care and diligence, we confirm that:

1. the factual disclosures in the report are accurate,
2. the consideration paid by the Company for the transactions listed in the report was not inappropriately high."

The Supervisory Board agrees with this opinion. Following the concluding findings of its review, the Supervisory Board has not expressed any reservations regarding the concluding statement by the Management Board in the report on relationships with affiliated companies.

The Supervisory Board would like to express its thanks and appreciation for the work of the Management Board and all employees in 2017.

Düsseldorf, April 26, 2018

ARAG SE

The Supervisory Board

Gerd Peskes
(Chairman)

Margit Schuler
(Deputy Chairwoman)

Professor Dr. Walter
Ackermann

Dr. Tobias Bürgers

Marco Hoogendam

Dr. Michael Pielorz

Professor Dr. Fred Wagner

Richard Wenhart

Dr. Sven Wolf

Governing Bodies of the Company

Supervisory Board

The employees have a right of codetermination pursuant to section 1 (1) of the German One-Third Participation Act (DrittelbG), under which one third of the members of the Supervisory Board must be employee representatives.

Supervisory Board Shareholder representatives:

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

Professor Dr. Walter Ackermann University professor,
St. Gallen, Switzerland

Dr. Tobias Bürgers Attorney,
Munich

Dr. Michael Pielorz Attorney,
Düsseldorf

Professor Dr. Fred Wagner University professor,
Leipzig

Dr. Sven Wolf Jurist,
Krefeld

Employee representatives:

Margit Schuler Chair of the Works Council of ARAG SE,
Mettmann,
Deputy Chairwoman

Marco Hoogendam Staff attorney,
Amersfoort, Netherlands

Richard Wenhart Employee in Production Management/
IT System Monitoring,
Buch a. Erlbach

Advisory Council	Christoph Buchbender	Member of the Management Board of Rheinland Holding AG, Neuss, Chairman
	Rainer Gebhart	Deputy Chief Executive Officer of WWK Lebensversicherung a. G., Rosenheim, Deputy Chairman
	Burkhard Balz	Member of the European Parliament, Stadthagen
	Professor Dr. Dres. h. c. Rolf Dubs	University professor, St. Gallen, Switzerland
	Werner Gremmelmaier	Member of the Management Board of uniVersa Lebensversicherung a. G., Neukeferloh
	Dr. Volker Himmelseher	Graduate in Business Administration, Pulheim
	Dr. Dr. h. c. Burkhard Hirsch	Attorney, Düsseldorf
	Friedrich-Wilhelm Metzeler	Attorney/ Graduate in Business Administration, Düsseldorf
	Volker Steck	Chief Executive Officer of Helvetia Versicherungen/ Directorate for Germany, Frankfurt
	Hans Schwarz	Chief Executive Officer of Stadtparkasse Düsseldorf (ret.), Düsseldorf
	André Wüstner	Federal Chairman of the German Army Association (DBwV), Montabaur

Management Board	Dr. Dr. h. c. Paul-Otto Faßbender	Düsseldorf, Chief Executive Officer
	Dr. Renko Dirksen	Meerbusch
	Dr. Johannes Kathan	Düsseldorf (until April 30, 2017)
	Dr. Matthias Maslaton	Moers
	Werner Nicoll	Herzogenrath
	Hanno Petersen	Ratingen
	Dr. Joerg Schwarze	Düsseldorf

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.

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You can find the latest **information about the Group and our products** on our website:
www.ARAG.com

Figures in this annual report are rounded, which may give rise to differences of +/- one unit (euros, percent) in some computations.

Credits

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