

ARAG SE

# 2017 Solvency and Financial Condition Report



Dive into life.

# ARAG Group

Asset and investment management

ARAG Holding SE

Operating Group Holding Company

ARAG SE

and legal insurance

CEO and Central Group Functions

Group Development/ Business Organization

Group Sales/ Products and Innovation

Group Finance

Group IT and Operations

Group Risk Management/ Controlling

Operating insurance companies

ARAG Allgemeine Versicherungs-AG

(Casualty and property insurance)

ARAG Krankenversicherungs-AG

(Health insurance)

Interlloyd Versicherungs-AG

(Specialized in broker sales)

International companies

(Legal insurance/ legal services)

Service companies

ARAG IT GmbH

(IT services for the ARAG Group)

Cura Versicherungsvermittlung GmbH

(Brokerage firm)

ARAG Service Center GmbH

(Emergency telephone service)

# Structure of ARAG SE

Company

ARAG SE

Members of the Management Board and areas of responsibility

**Central Group Functions and CEO**

Dr. Dr. h. c. Paul-Otto Faßbender

**Group Development/  
Business Organization**

Dr. Renko Dirksen

**Group Sales/  
Products and Innovation**

Dr. Matthias Maslaton

**Group Finance**

Werner Nicoll

**Group IT and Operations**

Hanno Petersen

**Group Risk Management/  
Controlling**

Dr. Joerg Schwarze

## Key Figures

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Gross premiums written:

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€ **870** million

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↗ 2016: € 825 million

Net income for the year:

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€ **32** million

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→ 2016: € 32 million

Combined ratio:

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**98.1**%

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↘ 2016: 95.8%

Eligible own funds:

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€ **1,175** million

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↘ 2016: € 1,314 million

Solvency capital requirement:

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€ **356** million

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↗ 2016: € 416 million

Solvency ratio:

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**329.9**%

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↗ 2016: 315.9%

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## Summary

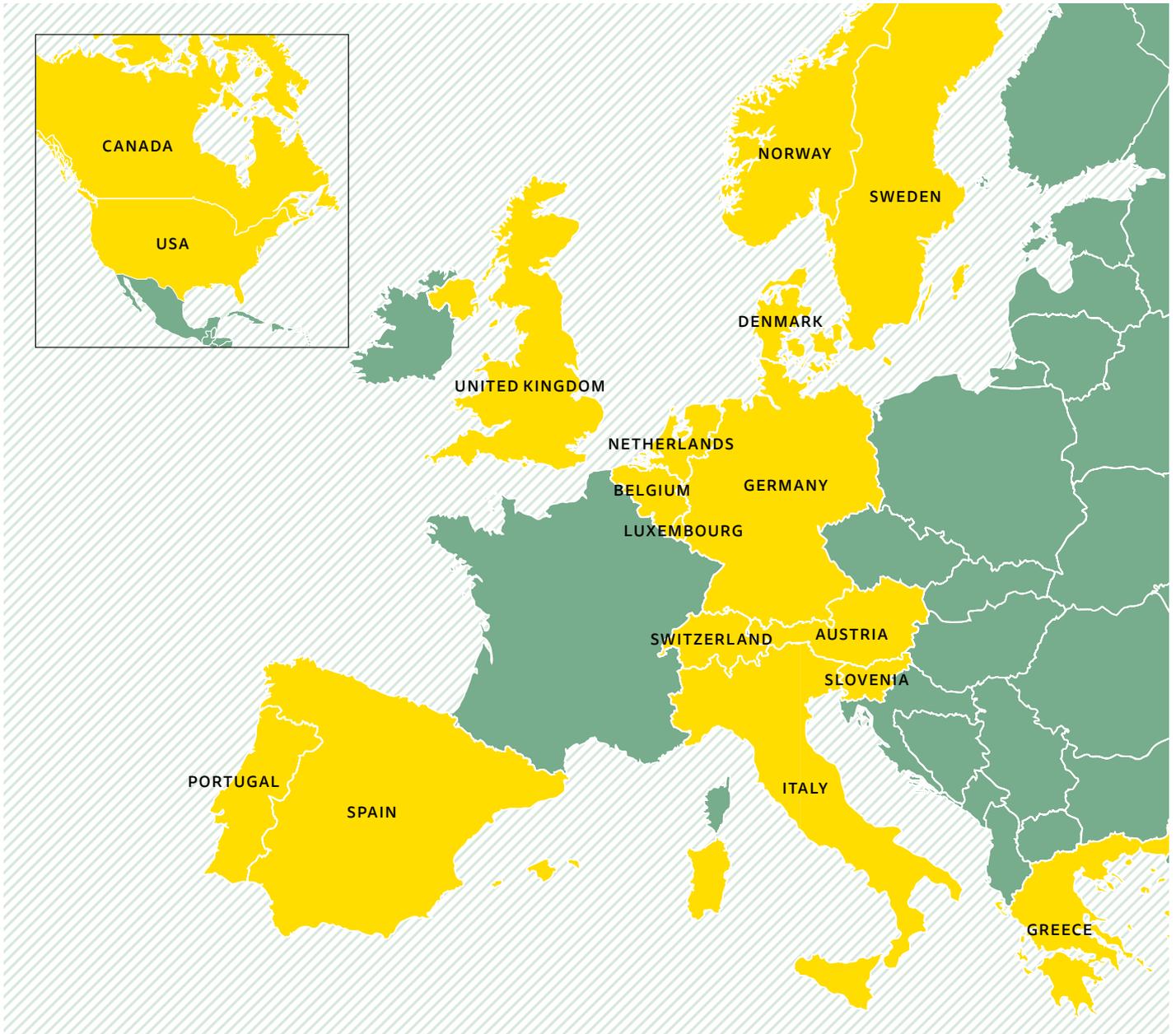
The ARAG Group is the largest family enterprise in the German insurance industry and is one of the world's three leading providers of legal insurance. ARAG was established more than 80 years ago exclusively as a legal insurance company, but has now positioned itself as an international insurer of considerable renown offering innovative, high-quality insurance products. At the end of 2016, the Group sold its shares in ARAG Lebensversicherungs-AG as part of a strategic realignment to focus squarely on property and health insurance business. This sale was completed in 2017. 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 approximately €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.

ARAG SE 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 is not involved in diversified corporate business with individual risks. Outside Germany, it also operates travel insurance business in connection with its provision of legal insurance.

In the period under review, ARAG SE increased its premiums by 5.5 percent to €870,004 thousand. It generated 59.9 percent of its total gross premium income outside Germany, making ARAG SE one of the most internationalized German insurers. The branches in the Netherlands, Spain, and Italy each earn more than €100,000 thousand in premiums and, partly because of their steady growth, count among the leading providers of legal insurance in their respective markets. However, the smaller branches in the Group are also successful. ARAG SE's branch in Greece, for example, has grown continuously despite the country's difficult economic situation and acts as a reliable partner to its customers when times are challenging.

In ARAG SE's important home market of Germany, the upswing in legal insurance business seen in previous years was further consolidated last year. In 2017, gross premiums written in direct business increased by 6.1 percent, from €329,272 thousand to €349,202 thousand. The underwriting result declined year on year, falling from a profit of €30,377 thousand in 2016 to €14,841 thousand in 2017. By contrast, net gains on investments remained at a high level. Despite the persistent environment of low interest rates,

## Countries in which the ARAG Group operates



they reached €73,016 thousand, which was just under 0.5 percent above the prior-year figure. The Company's net income for the year amounted to €32,031 thousand, a rise of 1.16 percent compared with 2016.

The new European regulatory regime, Solvency II (SII), came into force for all insurance companies on January 1, 2016 and is aimed at harmonizing regulation and affording customers greater protection. It contains rules on capital adequacy, risk management, and reporting. Valuations for solvency purposes are based on market values, whereas

under accounting rules pursuant to the German Commercial Code (HGB), assets are recognized at amortized cost in accordance with the prudence principle. Consequently, some parts of the report cannot be compared with each other. A reconciliation of the line items is provided in chapters D. 'Valuation for Solvency Purposes' and E. 'Capital Management'.

In a process lasting five years, ARAG SE made use of the options made available by the supervisory authorities and developed a partial internal model for which it obtained certification from the German Federal Financial Supervisory Authority (BaFin) in December 2015 in time for the start of Solvency II. ARAG SE is one of only a small number of German insurers that have successfully completed the certification process, which is a particularly good achievement given its size. As a result of approval being granted, the Company is able to measure its risks in a way that is tailored to its business and manage them accordingly in order to provide customers with greater protection. ARAG SE uses an internal model for market risk, non-life underwriting risk, and counterparty default risk. This enables the conservative investment policy and the interdependencies of the individual risk exposures to be reflected appropriately in the risk calculation. The modeling process also benefits from the expertise that has been accumulated over the course of more than 80 years of providing legal insurance with a clearly defined product and underwriting policy.

In connection with the introduction of Solvency II, ARAG SE has not only completely redesigned how it values risk but also updated its operational and organizational structure. It thus has a governance system with an appropriate structure and complexity that is based on the organization's relationship with the risks assumed. ARAG SE has implemented the following key functions in its organization as autonomous, independent functions: Compliance, Internal Audit, the Actuarial function, and Risk Management. In this regard, the Company has been guided by German legislation and also complies with European directives and recommendations from various bodies and organizations, as well as with internal policies governing processes, roles, and responsibilities.

ARAG SE's risk profile is shaped by the two internally modeled major risks: market risk and underwriting risk. The solvency capital requirement for market risk, which is the more dominant of the two, is €313,983 thousand. The drivers are equity risk, equity investment risk, and credit risk. Underwriting risk, for which the solvency capital requirement is €158,005 thousand, is mainly influenced by premium and reserve risk. ARAG SE's overall solvency capital requirement is €356,125 thousand. To cover the solvency capital requirement, ARAG SE has eligible own funds of €1,174,867 thousand, giving a coverage ratio of 329.9 percent. ARAG SE thus has a very high level of capital adequacy, a clear sign of the Company's excellent financial strength.

## A. Business and Performance

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## A.1 Business

### Legal basis

ARAG SE was founded on July 15, 1935 in Düsseldorf, Germany. It is entered in the commercial register of the Düsseldorf local court under the number HRB 66846. Its contact details are:

ARAG SE  
ARAG Platz 1, 40472 Düsseldorf, Germany

Tel: +49 (0)211 98 700 700  
Fax: +49 (0)211 963 2850  
Email: [service@ARAG.de](mailto:service@ARAG.de)  
Website: [www.ARAG.com](http://www.ARAG.com)

ARAG SE was entered in the commercial register as a European Company (Societas Europaea, SE) on December 1, 2011. This change in the legal form of the Company, which had previously been a stock corporation (Aktiengesellschaft, AG) called ARAG Allgemeine Rechtsschutz-Versicherungs-Aktiengesellschaft, Düsseldorf, was based on a resolution of the Annual General Meeting on October 19, 2011 in accordance with the transformation plan dated February 8, 2011.

### Supervisory authority

The contact details of the authority that supervises ARAG SE and the ARAG Group as a whole are:

Bundesanstalt für Finanzdienstleistungsaufsicht  
Graurheindorfer Strasse 108, 53117 Bonn, Germany  
Postfach 1253, 53002 Bonn, Germany

Tel: +49 (0)228 4108 0  
Fax: +49 (0)228 4108 1550  
Email: [poststelle@bafin.de](mailto:poststelle@bafin.de)  
De-Mail: [poststelle@bafin.de-mail.de](mailto:poststelle@bafin.de-mail.de)  
Website: [www.bafin.de](http://www.bafin.de)

### Auditor

The contact details of the appointed auditor are:

PricewaterhouseCoopers GmbH  
Wirtschaftsprüfungsgesellschaft  
Moskauer Strasse 19, 40227 Düsseldorf, Germany

Tel: +49 (0)211 981 0  
Fax: +49 (0)211 981 1000  
Email: [webkontakt\\_anfragen@de.pwc.com](mailto:webkontakt_anfragen@de.pwc.com)  
Website: [www.pwc.de](http://www.pwc.de)

### Structure of ARAG SE

Indirectly, ARAG SE is wholly owned by ARAG Holding SE, Düsseldorf, which directly holds a 50 percent equity investment. ARAG Holding SE has equity (in accordance with HGB) of €278,701 thousand. The members of the Management Board are Dr. Dr. h. c. Paul-Otto Faßbender, Dr. Sven Wolf, and Klaus Heiermann (since March 1, 2018). The second shareholder is AFI Verwaltungs-Gesellschaft mbH, Düsseldorf, which holds a 50 percent equity investment in ARAG SE. AFI Verwaltungs-Gesellschaft mbH has equity of €113,063 thousand and is represented by its Managing Directors Dr. Dr. h. c. Paul-Otto Faßbender and Dr. Sven Wolf. The existence of the majority interest was notified to ARAG Allgemeine Rechtsschutz-Versicherungs-AG (now ARAG SE) on April 28, 2000 by the governing bodies of the parent companies in accordance with section 20 (1) and (4) of the German Stock Corporation Act (AktG). ARAG SE is a dependent company within the meaning of section 17 (1) AktG in relation to ARAG Holding SE.

ARAG SE is responsible for the strategic Group management of the ARAG Group, whose parent company is ARAG Holding SE. The shareholders of ARAG Holding SE are FABI GmbH, Düsseldorf, which holds 45.5 percent, and Dr. Dr. h. c. Paul-Otto Faßbender personally, who holds the remaining 54.5 percent. ARAG Holding SE limits itself to exercising its rights and fulfilling its obligations as a shareholder in the investee companies. The ARAG Group comprises 45 Group companies, including six insurance companies headquartered in Germany, Norway, and the US.

### List of the main affiliated companies

Name	Legal form	Headquarters	Direct share	Group's share
1 ARAG Holding SE	SE	Düsseldorf	0.00%	Group parent company
2 AFI Verwaltungs-Gesellschaft mbH	GmbH (private limited company)	Düsseldorf	0.00%	100.00%
3 ARAG 2000 Grundstücksgesellschaft bR	GbR (partnership under the German Civil Code)	Düsseldorf	50.90%	94.90%
4 ARAG Allgemeine Versicherungs-AG	AG	Düsseldorf	100.00%	100.00%
5 ARAG Insurance Company Inc.	Corporation	Des Moines	0.00%	100.00%
6 ARAG International Holding GmbH	GmbH	Düsseldorf	100.00%	100.00%
7 ARAG IT GmbH	GmbH	Düsseldorf	100.00%	100.00%
8 ARAG Krankenversicherungs-AG	AG	Munich	94.00%	94.00%
9 ARAG North America Inc.	Corporation	Des Moines	0.00%	100.00%
10 ARAG Plc.	Plc.	Bristol	100.00%	100.00%
11 ARAG Service Center GmbH	GmbH	Düsseldorf	80.00%	100.00%
12 Cura Versicherungsvermittlung GmbH	GmbH	Düsseldorf	100.00%	100.00%
13 HELP Forsikring AS	AG	Oslo	100.00%	100.00%
14 Interlloyd Versicherungs-AG	AG	Düsseldorf	0.00%	100.00%

### Description of the main affiliated companies

1. ARAG Holding SE is the parent company of the ARAG Group from a company law perspective. It does not exercise influence in the sense of acting as an overarching Group management entity. The operational management of the ARAG Group is the responsibility of ARAG SE. As well as managing the equity investments, ARAG Holding SE rents out real estate.
2. AFI Verwaltungs-Gesellschaft mbH manages 50.0 percent of the shares in ARAG SE. This management remit is limited to exercising its rights and fulfilling its obligations as a shareholder in the equity investment.
3. ARAG 2000 Grundstücksgesellschaft bR manages the plot of land at ARAG Platz 1, 40472 Düsseldorf, where the ARAG Group's headquarters are located.
4. ARAG Allgemeine Versicherungs-AG operates the Group's casualty and property insurance business in Germany and through a branch in the United Kingdom. It is necessary to operate this business in a separate company because, in Germany, legal insurance claims have to be settled separately (section 164 of the German Insurance Supervision Act (VAG)). ARAG Allgemeine primarily offers modular insurance cover for general accident insurance, general liability insurance, and private property insurance (mainly composite residential buildings and home contents insurance) to private and small business customers. This company is also Europe's largest sports insurer, providing cover for over 20 million people – from those enjoying sport as a leisure activity right up to professional sportsmen and women.
5. ARAG Insurance Company, USA, operates legal insurance business, mainly through employers and trade associations. Insurance is provided to their employees and members, although coverage varies from state to state depending on the local regulatory rules. ARAG Insurance Company is part of a subgroup in the USA that comprises four companies and is managed by ARAG North America Inc.
6. ARAG International Holding GmbH is an intermediate holding company connecting the North American (US and Canadian) subsidiaries to the ARAG Group in Germany. It is purely a financial holding company without any managerial authority; it limits itself to exercising its rights and fulfilling its obligations as a parent company. Besides its function as a holding company, it is also responsible for winding up the business activities of the ARAG Group's discontinued operations.
7. ARAG IT GmbH, which is located at the Düsseldorf site, carries out all data center activities and IT services required by the ARAG Group. It only has a few customers outside the ARAG Group.
8. ARAG Krankenversicherungs-AG operates the private health insurance business. The need to separate the different segments (section 8 (4) VAG) means that a separate company has to operate the health insurance business. ARAG Krankenversicherungs-AG has established itself in its market as a provider of high-quality full-coverage and supplementary private health insurance.
9. ARAG North America Inc., USA, is the country-specific holding company for the ARAG Group's US business lines. It holds all of the shares in the four other US subsidiaries.

10. ARAG Plc., United Kingdom, works as an intermediary by brokering business with end customers and passing it on to primary insurers within and outside the ARAG Group. The bulk of claims settlement for the primary insurers is handled by ARAG Plc. itself.
11. ARAG Service Center GmbH is the customer service center for all German insurance companies in the ARAG Group, providing comprehensive assistance services and a telephone hotline around the clock. It also acts as a mediator in the resolution of legal disputes.
12. Cura Versicherungsvermittlung GmbH brokers insurance business to third parties that the ARAG Group does not underwrite itself. The company also takes care of the insurance requirements of the ARAG Group's own employees.
13. HELP Forsikring AS, Norway, primarily offers family legal insurance coverage for interest groups – predominantly labor unions – in Norway, Sweden, and Denmark. In Norway, it also offers a special legal insurance product for homebuyers.
14. Interlloyd Versicherungs-AG is a wholly owned subsidiary of ARAG Allgemeine Versicherungs-AG and, like its parent company, operates the casualty and property insurance business. Unlike its parent company, however, it operates its business through insurance brokers rather than directly. Interlloyd Versicherungs-AG also has a branch in Spain.

#### **Qualitative and quantitative disclosures on relevant events and significant intragroup transactions**

ARAG SE is responsible for the legal insurance operating business at both domestic and international levels and for strategic Group management. In this role, it holds material equity investments in Group companies, performs centralized services for the insurance companies in the Group, e.g. investment management, risk management, and personnel development, and manages major projects affecting various parts of the Group, e.g. modifying the accounting systems, designing the IT infrastructure. Significant events and transactions are listed below.

ARAG SE has a rental agreement with ARAG 2000 GbR concerning the rental of office space and ancillary areas at ARAG's headquarters in Düsseldorf. The rent and secondary costs were agreed upon on an arm's-length basis and, in 2017, amounted to €10,695 thousand. Service fees of €17,161 thousand were paid to ARAG IT GmbH in 2017 for data center operation, software solution development, and software maintenance.

Since June 2000, there has been a cash-pooling agreement between ARAG SE, which manages the cash pool, and the other Group companies in Germany. Under this agreement, all cash and cash equivalents held by the members of the cash pool are managed centrally by ARAG SE and invested in the money markets. Interest at money market rates is applied to the intercompany balances between the members of the cash pool arising from these transactions.

ARAG SE has contracts with the affiliated companies concerning the performance of services, insurance brokerage, the use of trademark rights, and support for and shared use of real estate, office furniture, and equipment. Most of these contracts were entered into before the establishment of the dependency on ARAG Holding SE and on the entities in which it holds a majority shareholding. All of the contracts have been concluded on arm's-length terms.

### **Line of business**

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.

The Company is a legal insurance provider focusing on private and small business customers. It is not involved in diversified corporate business with individual risks. Outside Germany, 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.

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.

As well as in the aforementioned international 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, under the unified management of ARAG SE in its role as parent company.

In addition, ARAG SE operates in Switzerland via equity investments in legal insurance associates. In the United Kingdom, a Group company acts as a broker for legal insurance business and legal-insurance-related special service package business, passing this business to four UK primary insurers. Some of this insurance is then ceded to ARAG SE under quota-share reinsurance treaties. This intermediary model has been adapted for use in the Canadian market, 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.

The breakdown of ARAG SE's 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
<b>Total</b>	<b>4,160,506</b>	<b>4,138,484</b>

#### Significant business or other events in the reporting period

Innovativeness is a key driving force for ARAG and one of its major strengths. Besides refining the portfolio, the Company has implemented new and groundbreaking ideas for products and services that are always geared to meeting customer requirements and creating benefits for them. 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.

Complementing these product innovations, virtually all of ARAG's international branches and companies have incorporated digital services such as live chat for policyholders and the ARAG WalletCard – which are already well established in the German market – as fixed components of their range of services. In 2017, accompanied by a great deal of publicity, the ARAG Group launched the ARAG travel assistant, the first advisory chatbot for insurance products on the German market. In no time at all, the chatbot was

successfully adapted by ARAG SE's branch in Spain. The ARAG Group is also constantly adding new pages to its websites. 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](http://www.ARAG.de). The groupwide transfer of knowledge and technology has proven itself to be invaluable as a successful model when designing international ARAG websites – further international websites have been optimized in this way and standardized in terms of branding.

Digitalization, a key theme in the Group, extends beyond digital services and IT system upgrades, however. 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.

In previous years, not least against the backdrop of persistently low interest rates, ARAG SE had already begun to reorganize the ARAG Group structure and decided to sell its shares in ARAG Lebensversicherungs-AG to Frankfurter Leben-Gruppe. When the shares in ARAG Lebensversicherungs-AG, Munich, were sold on June 30, 2017, as approved, the shares in ARAG Krankenversicherungs-AG were transferred to ARAG SE.

No further significant reportable events or transactions took place during the year under review.

## A.2 Underwriting 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 €868,041.4 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 as a result of the new discounting method, 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. 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.

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.

Based on the quantitative reporting required for regulatory purposes, the underwriting result for the reporting period amounted to €16,307 thousand. The following table shows this underwriting result with a reconciliation to the underwriting result in accordance with HGB, as published in the 2017 Annual Report and explained above.

### Underwriting result

(€'000)	2017	2016
Net premiums earned	868,041	814,252
Claims incurred (net, excluding claim settlement costs)	- 345,661	- 377,799
Changes in other technical provisions (net)	192	- 6
Insurance business operating expenses incurred and miscellaneous underwriting expenses (net)	- 506,265	- 401,979
<b>Underwriting result in accordance with template S.05.01.02</b>	<b>16,307</b>	<b>34,469</b>
Technical interest income	0	0
Miscellaneous underwriting income	1,683	1,465
Miscellaneous underwriting expenses (net)	- 71	0
<b>Underwriting result in accordance with HGB*</b>	<b>17,919</b>	<b>35,933</b>

\* Underwriting result before change in the equalization provision and similar provisions

ARAG SE's underwriting result is generated in Germany and other countries from three classes of insurance within the overall property insurance business. The structure of the presentation follows that of template S.05.01 in the Appendix. The items are valued according to HGB principles, whereas the structure is in accordance with Solvency II requirements. The breakdown of the components of the underwriting result can be found in template S.05.01. The expenses incurred are stated after the allocation to the functional areas 'Services' and 'Company as a whole'. Claim settlement costs are included in the stated 'Expenses incurred' and are aggregated under 'Insurance business operating expenses incurred and miscellaneous underwriting expenses (net)'.

The factors that have contributed to the change in the underwriting result are described in the preceding two pages of this chapter. The following table shows a breakdown of the underwriting result by main line of business:

#### Underwriting result by main line of business\*

(€'000)	Net premiums earned	Claims incurred (net, excluding claim settlement costs)	Change in sundry technical provisions (net)	Insurance business oper- ating expenses incurred and miscellaneous underwriting expenses (net)	Underwriting result	Underwriting result
					2017	2016
Legal insurance	796,227	309,537	192	471,014	15,867	35,704
Travel insurance	61,453	36,290	0	29,080	-3,917	-4,819
Miscellaneous insurance	10,361	-166	0	6,171	4,356	3,584
<b>Total</b>	<b>868,041</b>	<b>345,661</b>	<b>192</b>	<b>506,265</b>	<b>16,307</b>	<b>34,469</b>

\* In accordance with template S.05.01.02

The legal insurance business is operated in Germany and other European countries. Travel insurance business is only operated in Spain and Portugal. Miscellaneous insurance business mainly comprises supplementary financial assistance benefits and is only offered in Spain, Portugal, and Italy. The following table shows a breakdown of the underwriting result by geographical area:

#### Underwriting result by main geographical area\*

(€'000)	Net premiums earned	Claims incurred (net, excluding claim settlement costs)	Change in sundry technical provisions (net)	Insurance business oper- ating expenses incurred and miscellaneous underwriting expenses (net)	Underwriting result	Underwriting result
					2017	2016
Germany	367,198	206,750	221	187,258	-26,589	-6,856
Netherlands	148,343	23,038	0	111,746	13,560	14,034
Spain	137,771	57,198	0	73,392	7,181	6,128
Italy	121,505	30,632	0	87,050	3,823	3,667
Other areas	93,224	28,043	-29	46,812	18,332	17,496
<b>Total</b>	<b>868,041</b>	<b>345,661</b>	<b>192</b>	<b>506,265</b>	<b>16,307</b>	<b>34,469</b>

\* In accordance with template S.05.01.02

### A.3 Investment Performance

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.

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. 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 in an amount of €391.0 thousand were required. 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 €73,015.9 thousand in the year under review compared with €72,678.6 thousand in 2016.

The net gains and losses on investments\* in accordance with HGB in the year under review amounted to a net gain of €73,016 thousand, representing a net yield on investments\*\* of 3.9 percent.

\* Administrative expenses are included in the net gains and losses

\*\* Calculation of net yield: net gain or loss on investments (including administrative expenses)/average investment portfolio value

The following table shows the breakdown of ARAG SE's gains and losses on investments in accordance with HGB\*\*\* by individual asset class as required by Solvency II:

### Gains and losses on the investments of ARAG SE

Type of investment (€'000)							Change in gains and losses	
	Current income	Realized gains	Realized losses	Reversals of write-downs	Depreciation, amortization and write-downs	Current expense/loss transfers	Gains and losses on investments in 2017	Gains and losses on investments in 2016
Property, plant & equipment held for own use	0	0	0	0	816	0	-816	0
Property (other than for own use)	6,089	16	26	0	1,623	0	4,456	7,336
Holdings in related undertakings, including participations	39,272	0	0	0	391	0	38,881	26,509
Equities – listed	28	0	0	91	0	0	119	-21
Equities – unlisted	0	0	0	0	0	0	0	0
Government bonds	4,168	36	150	33	554	0	3,533	5,341
Corporate bonds	10,552	80	304	157	978	0	9,507	11,633
Structured notes	0	0	0	0	0	0	0	0
Collateralized securities	606	123	3	0	7	0	719	743
Collective investment undertakings	19,018	1,281	0	3,806	880	0	23,225	26,882
Derivatives	0	0	0	0	0	0	0	0
Deposits other than cash equivalents	1	0	0	0	0	0	1	42
Other investments	448	0	116	0	356	0	-24	369
Deposits to cedants	184	0	0	0	0	0	184	155
Cash and cash equivalents	0	0	0	0	0	0	0	0
Current expense (unallocated)/loss transfers	0	0	0	0	0	-6,769	-6,769	-6,310
<b>Total</b>	<b>80,366</b>	<b>1,536</b>	<b>599</b>	<b>4,087</b>	<b>5,605</b>	<b>-6,769</b>	<b>73,016</b>	<b>72,679</b>

### Information on securitization instruments

Investments in securitization instruments also make a contribution to investment performance. As defined in HGB accounting rules, this category of investments mainly comprises instruments such as asset-backed securities and mortgage-backed securities. Pfandbriefs, on the other hand, are not classified as investments in securitization instruments because they are treated as corporate bonds.

From a Solvency II perspective, ARAG SE held asset-backed securities and mortgage-backed securities with a value of €9,675 thousand as of the reporting date.

\*\*\* The total of the gains and losses on investments presented in the table equates to the gains and losses on investments published in ARAG SE's 2017 Annual Report.

## A.4 Performance of Other Activities

Other net income/expense includes staff costs and general and administrative expenses that were not allocated to an insurance or investment-related function in accordance with function-based accounting (distribution of secondary costs). These are expenses that are incurred on behalf of the Company as a whole (e.g. remuneration for members of supervisory bodies, the auditor's fees, general costs for legal advice and tax advice, interest expense for hybrid capital and for provisions for pensions and other post-employment benefits) or that arise from the performance of services for other Group companies and third parties. The following table provides an overview of other net income/expense:

<b>Other income</b>			
(€'000)	2017	2016	Change
Income from insurance brokerage	37,929	36,981	948
Income from services	39,258	39,840	-582
Income from sub-letting of premises	3,298	3,305	-7
Income from the reversal of provisions	3,467	2,619	848
Miscellaneous income	14,182	7,175	7,007
<b>Total</b>	<b>98,134</b>	<b>89,920</b>	<b>8,214</b>

<b>Other expenses</b>			
(€'000)	2017	2016	Change
Expenses for services	83,914	84,320	-406
Interest expense and similar charges (interest cost from unwinding of discounts, interest on taxes)	8,824	6,720	2,104
Expenses incurred on behalf of the Company as a whole	26,177	23,080	3,097
Sundry expenses	10,285	10,828	-543
<b>Total</b>	<b>129,200</b>	<b>124,948</b>	<b>4,252</b>
<b>Other net income/expense</b>	<b>-31,066</b>	<b>-35,028</b>	<b>3,962</b>

### Information on leases

A distinction is made between finance leases and operating leases. ARAG SE is a lessee under leases that are accounted for as operating leases. It is not involved in any material finance leases. The operating leases mainly relate to company cars and cellphones used by employees of ARAG SE. As lessee, ARAG SE recognizes the lease payments as an expense.

## A.5 Any Other Information

Chapters A.1 to A.4 inclusive contain all of the important information about business and performance.

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## B.1 General Information on the System of Governance

ARAG SE's clear corporate objectives and the strategy aimed at achieving them provide a clear operational framework both for senior management and for employees. At the same time, they enable each employee to make his or her own valuable contribution to achieving the objectives. The strategy and objectives were developed in collaboration with senior management and are consistent with the overarching business idea.

This idea – 'Every individual should be able to assert his or her legal rights – irrespective of his or her financial situation' – was defined more than 80 years ago. It remains enshrined in every area of ARAG SE's business to this day and has therefore always been what motivates the Company.

The ARAG Group and its German companies have a dual management and control system comprising the Supervisory Board and Management Board. A transparent organizational structure with clearly defined roles and responsibilities provides the optimum framework for the successful implementation of the business strategy. The main responsibilities, together with the related processes and reporting lines, have been documented in writing and agreed upon with the relevant committees at the different levels. The documentation can be accessed by those who need to use it. The resulting guidelines are reviewed at least once a year to ensure that they are up to date and are actively communicated.

In terms of scope, the operational and organizational structure reflects the business lines and areas. The sales channel mix, the extent of the different underwriting risks, and the degree of internationalization all play an important role in this regard.

The Group encourages a culture in which risk is actively embraced as well as a strong understanding of risk at all levels. The deliberate assumption of risk is of course part of an insurance company's business activities. Continual refinements in all areas are necessary in order to manage this process successfully, not only for the Company but also for customers. This affects firstly the risks assumed, which evolve in a constantly changing environment and require the Company to develop new solutions over time. But the Company and the organization itself are also exposed to processes of continual change and development, particularly as a result of regulation, the market environment, and the competitive situation. ARAG provides continuing professional development (CPD) activities – both internal and external – for all employees and all senior managers to ensure that the organization is always equipped to rise to the latest challenges and can proactively tackle emerging risks.

The Company also ensures that employees always have the necessary knowledge and information about processes to be able to carry out their tasks properly. They are assisted in this by an information system that provides comprehensive, robust, clearly defined, consistent, timely, and relevant data on the various business activities and on the related risks that are deliberately assumed. Moreover, the clear reporting lines ensure that information is communicated promptly in such a way that those receiving it are able to immediately recognize the significance of the information and formulate the necessary steps to be taken in their area of responsibility. The security, completeness, and confidentiality of the information are of course maintained at all times.

The Company has structured its system of governance in such a way that its business activities can be managed soundly and conservatively in line with the business and risk strategies. As part of its overall responsibilities, the Management Board ensures that there is an orderly system of governance in place, so that it:

- Is effective, is fit for purpose, and – in terms of its nature, scope, and complexity – is commensurate with the Company's business activities
- Ensures compliance with laws, regulations, and regulatory requirements
- Ensures sound and prudent management of the Company
- Has an adequate, transparent organizational structure with clearly allocated and separated responsibilities
- Has an effective inhouse communications system
- Is regularly reviewed.

The responsibilities of the Management Board of ARAG SE are organized as follows: Central Group Functions, Finance, IT and Operations, Group Development and Business Organization, Group Risk Management and Group Controlling, and Group Sales, Products and Innovation. Each area of responsibility is assigned to a specific member of the Management Board.

Together with the Management Boards of the other companies, the Management Board of ARAG SE has set up the Risk Committee to help it fulfill its risk management duties. To ensure the regulatory requirements concerning the use of a partial internal model are met in day-to-day operations, the Risk Committee has set up a subcommittee, the Internal Model Committee.

ARAG SE does not currently have an independent remuneration committee in accordance with article 275 (1) (f) of Delegated Regulation (EU) 2015/35 (the Delegated Regulation). The size of the Company (particularly the number of employees) in relation to the internal structure means that, at the moment, the organization itself is able to help the Management Board and the Supervisory Board supervise the remuneration guidelines and policies as well as the way they are put into practice and how they function.

The Supervisory Board is responsible for appointing and monitoring the Company's Management Board. To facilitate the decision-making process, the Supervisory Board has delegated individual tasks to the Finance Committee, Accounting and Audit Committee, and Human Resources Committee.

By the nature of its remit, the Finance Committee deals mainly with investment decisions and fundamental strategic decisions on asset allocation. The Finance Committee also deliberates on business decisions involving the portfolio of the Group companies.

The Accounting and Audit Committee primarily discusses the projections and forecasts presented to them over the course of the fiscal year that relate to the financial statements. It also examines the overall strategic planning at the preparation stage.

By the nature of its remit, the Human Resources Committee deliberates primarily on personnel matters relating to the members of the Management Board. As well as appointing, dismissing, and reappointing Management Board members, this also involves discussing the remuneration system, target achievement, and evaluation of targets.

The establishment of controls in the Company lies at the heart of the system of governance. These controls are mainly carried out by the four key functions: Risk Management, Compliance, Internal Audit, and the Actuarial function. As these functions are kept strictly separate from the operational departments as far as Management Board level, they can perform their duties objectively and independently. Moreover, they have a direct reporting line to the ARAG SE Management Board member with relevant responsibility and can also communicate directly with the Supervisory Board. The employees in these functions have the knowledge they need to be able to carry out their tasks adequately.

### **Risk management**

The tasks of the independent risk control function are performed by the Group Risk Management Central Department. As part of the risk management system that is in place, this department is responsible for the risk management process, which includes submitting regular reports to the Management Board. Its work does not include the operational management of risks, which is carried out directly by the relevant managers and process owners in compliance with internal rules. All risk-relevant decisions to be made by the Management Board take into account the information and opinions of the Group Risk Management Central Department.

### **Compliance**

The tasks of the compliance function are performed by the Group Legal/Compliance Central Department. The main compliance task is to draw up guidelines and policies designed to ensure legal requirements are fulfilled and corporate objectives are achieved. Responsibility for implementing the guidelines and policies lies with the individual managers. The Chief Compliance Officer advises the Management Board on compliance with laws and administrative regulations and submits regular reports to the Management Board on his or her work.

### **Internal audit**

Internal audit tasks are performed by the Group Audit Central Department, which is a process-independent function that examines and assesses structures and activities within the Group. This auditing is carried out on behalf of the Management Board and covers all processes relating to business operations. The Group Audit Central Department has to assess and evaluate the integrity, propriety, effectiveness, efficiency, and adequacy of the internal control system (ICS). Audit findings are presented to the members of the Management Board in the form of an audit report.

### Actuarial function

The Actuarial Function department is responsible for the actuarial functions. It operates at an overarching level and reports directly to the Chief Risk Officer. The Chief Risk Officer is a member of the Management Board of ARAG SE and responsible for Group Risk Management and Group Controlling. The Actuarial Function department is essentially responsible for verifying the methodology used to calculate the technical provisions and for ensuring the adequacy of the underwriting and reinsurance policies. This includes verifying the methods applied, the assumptions made, and the data used as well as validating the partial internal model. The department submits reports on its findings to the Management Board and the supervisory authority.

### Information on remuneration guidelines and policies

As a core element of the Company's system of governance, the remuneration of the members of the governing bodies – and that of all those working for the Company – is based on the principles of appropriateness and transparency and is focused on sustainability.

This includes ensuring that the remuneration of members of governing bodies and employees is consistent with market rates and individual performance, and therefore appropriate. Those responsible for remuneration in the Company monitor remuneration levels in the relevant market and make adjustments accordingly, taking account of the performance of the individual employees and members of the governing bodies.

Transparency means that the general principles of the remuneration policy are disclosed to all employees. But it also means that the remuneration structures are designed to be only as complex as necessary and as simple as possible.

Sustainability is ensured by adequately aligning the remuneration structure with the Company's business strategy and risk profile.

Risks for the Company arising in relation to remuneration are managed effectively. For example, particular attention is paid to avoiding, as far as possible, any conflicts of interest that could arise between the individual tasks assigned to an employee or member of a governing body and their remuneration structure. Suitable measures are also put in place in advance to prevent such risks materializing.

The remuneration of the Company's **Management Board members** comprises a fixed basic salary and a variable element and is in line with regulatory requirements. In particular, the basic salary is set at a level that ensures the members of the Management Board are not heavily reliant on the variable component. This is especially important to ensure that the variable component rewards good performance but does not create such a significant incentive that it could encourage actions counter to the interests of the Company.

The variable element is equivalent to a percentage of the basic salary. No share plans or share option programs are offered anywhere in the ARAG Group. Against this background and with a view to ensuring that the Company offers attractive, market-level remuneration, the variable element of the remuneration for Management Board members is set at a maximum of 60 percent of basic salary and is subdivided into short-term

and long-term components. The long-term component equates to 60 percent of the aforementioned variable remuneration and, in accordance with article 275 (2) (c) and (f) of the Delegated Regulation, is deferred and takes into account the outcome of a review to establish whether there is any requirement for a potential downward adjustment as a result of exposure to current or future risks.

The targets relevant to variable remuneration are based on a mixture of objective Group and Company key performance indicators drawn from the strategic planning and of individual targets for each member of the governing body. The weighting of the targets is defined beforehand. Target achievement in respect of each target is capped at predefined limits. The variable remuneration never exceeds the basic salary.

If members of the Management Board of ARAG SE simultaneously hold Management Board or senior management positions in subsidiaries of ARAG SE, they do not receive any additional remuneration for these activities. However, such multiple roles can be acknowledged in the various categories within target agreements related to the variable remuneration granted under the principal employment contract. In this case, particular attention is paid to ensuring that this does not give rise to conflicts of interest.

If an individual does hold such multiple positions or fulfill multiple roles, a proportion of the costs is passed on to the relevant company by the company responsible for paying the remuneration.

If members of the Management Board of ARAG SE are also members of a Supervisory Board or administrative board of a subsidiary of ARAG SE, they receive fixed remuneration for these activities, but this remuneration is offset against the remuneration for the Management Board activities.

**Members of the Supervisory Board** of ARAG SE only receive fixed remuneration for their activities; the amount is specified in accordance with the articles of incorporation.

Unless **employees** of insurance companies in the Group are granted variable remuneration components under a pay agreement or other collective agreement on a non-discretionary basis, employees only receive such variable remuneration when they reach a certain management level. The variable remuneration for these managers is based on annual target agreements, which include a mix of objective Group and division key performance indicators and individual targets. The variable element is equivalent to a percentage of the basic salary and varies between 5 percent and 50 percent, depending on management level, function, and country.

The variable remuneration never exceeds the relevant basic salary. Target achievement is capped at predefined limits. The basic salary for the postholder concerned is set at an appropriate level to ensure that he or she is not substantially dependent on the variable remuneration components. Once again, the variable remuneration must encourage good performance but not create such a significant incentive that it could encourage actions counter to the interests of the Company.

The structure of the variable remuneration granted to the **CEOs of the Company's branches in the European Economic Area (EEA)** is based on the same principles used for the members of the Management Board, whereby the proportion of basic salary and/or the proportion for the long-term component may differ according to the postholder and, in particular, the size of the branch, the business activities, and standard practice in the country concerned.

In such cases, the mix of the targets applicable for the purposes of the variable remuneration also includes targets for the branch headed by the person in question.

Variable remuneration granted to individuals responsible internally for **key functions** follows the general principles for managers described above, although further requirements specified by BaFin in this regard have also been or are being implemented.

If persons responsible for key functions at ARAG SE also carry out functions outsourced by subsidiaries to ARAG SE, these individuals do not personally receive any additional remuneration in return for this work.

The Company grants **members of the Management Board** and their surviving dependants rights to a retirement pension, a widow's/widower's pension, and an orphan's pension. The retirement pension is calculated as a percentage of pensionable salary, which equates to the basic salary (excluding bonuses, remuneration in kind, etc.). There is also a cap on the absolute maximum amount. The widow's/widower's pension is equivalent to two-thirds of the retirement pension; the orphan's pension for each child is equivalent to one-third of the widow's/widower's pension. The total of the surviving dependants' pensions is limited to the amount of the retirement pension.

No early retirement arrangements have been made with Management Board members. However, the Company is entitled to make them retire five years before the standard retirement age with the contractually agreed deductions. The Management Board members do not have a corresponding right themselves.

The remuneration details set out for Management Board members who simultaneously fulfill roles for the subsidiaries of ARAG SE apply mutatis mutandis to pension and early retirement agreements.

**Supervisory Board members** do not receive any supplementary pensions.

Persons responsible for other **key functions** and CEOs of EEA branches receive an occupational retirement pension, the amount and extent of which is determined by the management level of the person concerned as well as by the statutory requirements and standard market practice where the job is located.

No early retirement arrangements have been made.

In the period under review, there were no material transactions with shareholders, persons able to exercise significant influence over the Company, or members of the administrative, management, or supervisory bodies. No significant changes were made to the system of governance in the reporting period.

## B.2 Fit and Proper Requirements

The ARAG Fit&Proper guidance specifies requirements, responsibilities, and processes to ensure that the members of governing bodies, CEOs of the Company's EEA branches, other postholders in key functions, and their employees are always professionally and personally suitable ('fit and proper') for the roles concerned. The main points are set out below.

### Management Board members and CEOs of EEA branches

To ensure they are fit for the role in terms of their professional suitability, members of the Management Board are required to have the professional qualifications, knowledge, and experience that ensures they can manage the Company soundly and prudently at all times. This calls for adequate theoretical and practical knowledge of insurance business and, in the case of managerial tasks, for sufficient leadership experience. Management Board members must be familiar with all of the material risks to which the Company is exposed and must be able to assess their potential impact.

Besides having the essential expertise in the individual areas for which each Management Board member is responsible, the Management Board as a whole must, as a minimum, have knowledge, skills, and experience pertaining to insurance and financial markets, business strategy and business models, the system of governance, financial analysis and actuarial analysis, the regulatory framework, and the regulatory requirements. Each individual member of the Management Board is expected to have not only specialist knowledge of the areas for which he or she is responsible but also adequate knowledge in all of the aforementioned areas. This is so that they can monitor each other's work.

Many years of experience working in the insurance industry or in another financial services company are crucial requirements for this role, as are managerial experience and the willingness to undertake continuing professional development.

The aforementioned qualifications also apply to the CEOs of the Company's various branches in the EEA *mutatis mutandis*, i.e. they must also have in-depth knowledge of the insurance and financial markets, business strategy and business models, the system of governance, financial analysis and actuarial analysis, the regulatory framework, and the regulatory requirements. However, this knowledge must relate primarily to the particular branch for which they are responsible. They also need to know about the domestic market in which their branch operates.

One standard benchmark is used to assess whether members of governing bodies, CEOs of EEA branches, and other people in key functions are personally suited to their role. Someone is assumed to be of good repute ('proper') if there is nothing to indicate the contrary. Someone is assumed not to be of good repute if, based on general life experience, his or her personal circumstances justify the assumption that these circumstances might negatively affect the careful and proper performance of his or her role or of the

tasks assigned to him or her. The factors considered are personal behavior and business conduct with regard to criminal-law, financial, property-law, and regulatory aspects. The laws of both Germany and other jurisdictions apply.

The Company's Supervisory Board assesses whether a potential Management Board member meets the 'fit and proper' requirements. This assessment is based not only on personal interviews but also on the candidate's CV – which should be informative and, in particular, contain details of all of his or her previous jobs – and associated documents. Good repute is checked by obtaining a criminal records check and an extract from the central register of companies and by having the candidate complete, sign, and submit to the Company a form requesting details about his or her good repute.

The Company's Management Board assesses whether Branch CEOs meet the 'fit and proper' requirements. In other respects, the information pertaining to Management Board members applies *mutatis mutandis*.

### **Supervisory Board members**

The members of the Supervisory Board must have the necessary knowledge, skills, and experience to be able to perform their monitoring role. They must always have the expertise needed to adequately monitor and oversee the Management Board and to actively support the Company's growth. Each member must therefore understand the Company's business and be able to assess the relevant risks. He or she must also be familiar with the main statutory requirements applicable to the Company. The individual members are not required to have specialist knowledge. However, they must be capable of identifying when they need to take advice and of obtaining this advice. In any case, the expertise of the Supervisory Board as a whole must cover investments, underwriting, and financial reporting. Having the necessary professional suitability entails undertaking continuing professional development.

Before the Annual General Meeting appoints someone to the Supervisory Board, both the potential Supervisory Board member and the Supervisory Board that proposed the candidate are expected to make sure that the potential member is sufficiently qualified. The special requirements published by BaFin apply to employee representatives.

With regard to the assessment of whether someone is of good repute, the information pertaining to Management Board members/Branch CEOs applies *mutatis mutandis*.

### **Other key functions**

The people responsible for key functions must have extensive knowledge and many years of experience of working in their particular field. All individuals in such roles must also be familiar with the legal parameters relevant to their position, the Company's organization and system of governance, and ARAG's business model. In addition, the people in key functions must have very good knowledge of the relevant operating processes, business systems, and the insurance industry.

The minimum initial requirements in terms of specialist expertise for any appointment to a role with internal responsibility for a key function are described below:

- Risk management: Actuarial or business management skills and qualifications or comparable academic qualifications are required. In particular, persons appointed to such roles are expected to have in-depth knowledge of relevant risk parameters, risk types, and valuation methods applicable to insurance business. Knowledge of all regulatory requirements pertaining to risk management is absolutely essential.
- Actuarial function: An individual responsible for this key function must have very well-honed actuarial and financial mathematics expertise together with a good level of business management knowledge. This expertise is normally acquired through a university degree in mathematics or through comparable training. The person concerned must also be a member of the German Actuarial Association (DAV), be able to provide evidence of equivalent professional status, or be prepared to combine work with study to obtain DAV membership or equivalent professional status.
- Compliance: The postholder must have a university degree in law or business management as well as specialist compliance expertise evidenced by professional development documentation or previous employment in this area of activity. He or she must continually keep abreast of statutory requirements and be able to demonstrate expertise, in particular, in the following areas: regulation, company law, and capital markets law, as well as competition and antitrust legislation.
- Internal audit: To ensure he or she is fit for the role in terms of professional suitability, the person responsible for this key function must hold a university degree in economics or business administration, or have undergone equivalent training, and must be able to demonstrate professional experience built up over many years. He or she must also have knowledge of the insurance industry, financial reporting, and business organization. In-depth know-how relating to auditing standards, auditing methodology, and audit-related software is a further prerequisite.

In all cases, people responsible for key functions must have a sufficient level of management experience for these positions. Because of the overlapping nature of many areas of the business, it is important that they have not only extensive knowledge of the work carried out in their own central department but also adequate knowledge of other departments with which they come into contact. It is essential that they are willing to undertake continuing professional development.

Job applicants must submit a detailed CV so that their career history and relevant previous experience can be examined. For both internal and external candidates, recruitment is based on a structured assessment process in which internal and external auditors assess their specialist and interdisciplinary qualifications in an assessment center. Each candidate's professional suitability is assessed individually, taking all the circumstances into consideration. The Management Board of the individual company is responsible for assessing whether people in key functions meet the 'fit and proper' requirements.

If outsourcing officers are appointed, the same fundamental requirements apply. However, the critical factors here are the requirements profile and, particularly in the case of internal candidates, relevant prior experience.

With regard to the assessment of whether someone is of good repute, the information pertaining to Management Board members/Branch CEOs applies *mutatis mutandis*.

It is the responsibility of those holding the remit for the relevant key function to assess the professional suitability of the employees working in the function or of candidates for relevant positions on the basis of suitable documentation or the day-to-day work carried out by the employee and to ensure that employees undertake regular professional development so that they always have the expertise they need to carry out their tasks. It is also the responsibility of employees themselves to keep up to date with the latest information. Professional development activities are documented.

With regard to the assessment of whether the people responsible for key functions and the employees working in these functions are of good repute, the same standard applies.

### **Continuing professional development as an ongoing process**

The responsible departments in the Company check whether all of the aforementioned members of governing bodies and postholders undertake the continuing professional development necessary to satisfy the requirements of their position. The professional development activities undertaken are documented in detail.

### **Cause for reassessment**

ARAG's Fit&Proper guidance defines circumstances that will result in a reassessment of whether someone is deemed 'fit and proper'.

The general rule regarding professional suitability is that the type and extent of any action to be taken by the Company depend on the supposed/actual shortcoming of the individual member of a governing body or holder of a key function. For example, he or she may be asked to undergo further training in a particular subject area. In extreme cases, however, the Company may consider removal from office or dismissal.

Doubts about personal suitability are investigated without delay. If there are circumstances that, based on general opinion, indicate that someone is not of good repute, the appropriate people within the Company will take immediate action. This action depends on the specific case in question and, above all, on the severity of the alleged or proven misconduct and may be temporary or permanent.

## B.3 Risk Management System Including the Own Risk and Solvency Assessment

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

Based on the 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, as a member of the Management Board of ARAG SE, is responsible for the implementation of the risk management system in all Group companies. Group Risk Management bears process responsibility for the risk management system and, by means of quarterly risk reports to the Management Board, ensures that there is comprehensive transparency with regard to the risk position and any changes to the risk position. Group Risk Management is also responsible for refining the risk management system and for drawing up proposals for uniform standards to be applied throughout the Group. The remit of the central department also includes developing models for determining risk-bearing capacity, solvency capital requirements, and the allocation of solvency capital.

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

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

**Risk identification**

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

**Risk analysis**

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

**Risk assessment**

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

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

**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 continual basis.

### **Own risk and solvency assessment (ORSA)**

The annual review of the ORSA policy provides the starting point for all regular ORSA processes. The policy sets out the guidelines for each ORSA process. A risk analysis of strategic positioning is then carried out; this takes the form of a bottom-up assessment by the managers involved.

The second risk analysis examines the Solvency II balance sheet, which provides the input for calculating the solvency capital requirements (SCR) and serves as the basis for projecting the balance sheet line items and related solvency capital requirements.

The result is a ranking of the identified risks. For the sake of completeness, the risk model used is also assessed on the basis of the results from validating the internal models and from assessing the assumptions used in the standard formula.

The Management Board is actively involved in the ORSA process. Using the budgeted figures signed off by the Management Board, the Solvency II balance sheet and the solvency capital requirements are projected beyond the strategic planning period. The results of the risk analysis and the projections are used to determine the overall solvency requirement.

All results are aggregated in the ORSA report and signed off by the Management Board. Once approved, the report is sent to all the relevant responsible parties so that they can incorporate the results into their decision-making processes.

The ORSA process is the link between the risk management system and the Company's capital management. The ORSA report describes the extent to which the Company can maintain its risk profile over the planning horizon. The comparison between the overall solvency capital requirement and eligible own funds provides an indication of future coverage. The Management Board can then use this information to assess whether there may be a need for action regarding the level and structure of own funds and the structure of the risk profile. This may involve the implementation of measures related to capital management and/or adjustments to the risk management system. In addition to workshops at which the Company's strategic positioning is discussed with the Management Board members, the Management Board also makes decisions on key elements of the ORSA process (e.g. stress tests). The Management Board is thus always aware of relevant developments affecting the risk profile. In the event of a significant change to the risk profile, the Management Board can trigger an ORSA process on an ad hoc basis.

#### **Governance of the partial internal model**

The Management Boards of the companies in the ARAG Group have formed a Risk Committee (RiCo) in order to incorporate the partial internal model into corporate management. The Risk Committee's main task is to assist the individual Management Boards with performing their risk management tasks in accordance with all statutory and internal requirements. In particular, this includes the establishment and monitoring of the group-wide risk management system. To ensure the regulatory requirements concerning the use of a partial internal model are met in day-to-day operations, the Risk Committee has set up a subcommittee, the Internal Model Committee (IMC). The Risk Committee and Internal Model Committee act in both an advisory capacity and a decision-making/monitoring capacity that are clearly defined in internal policies and guidance.

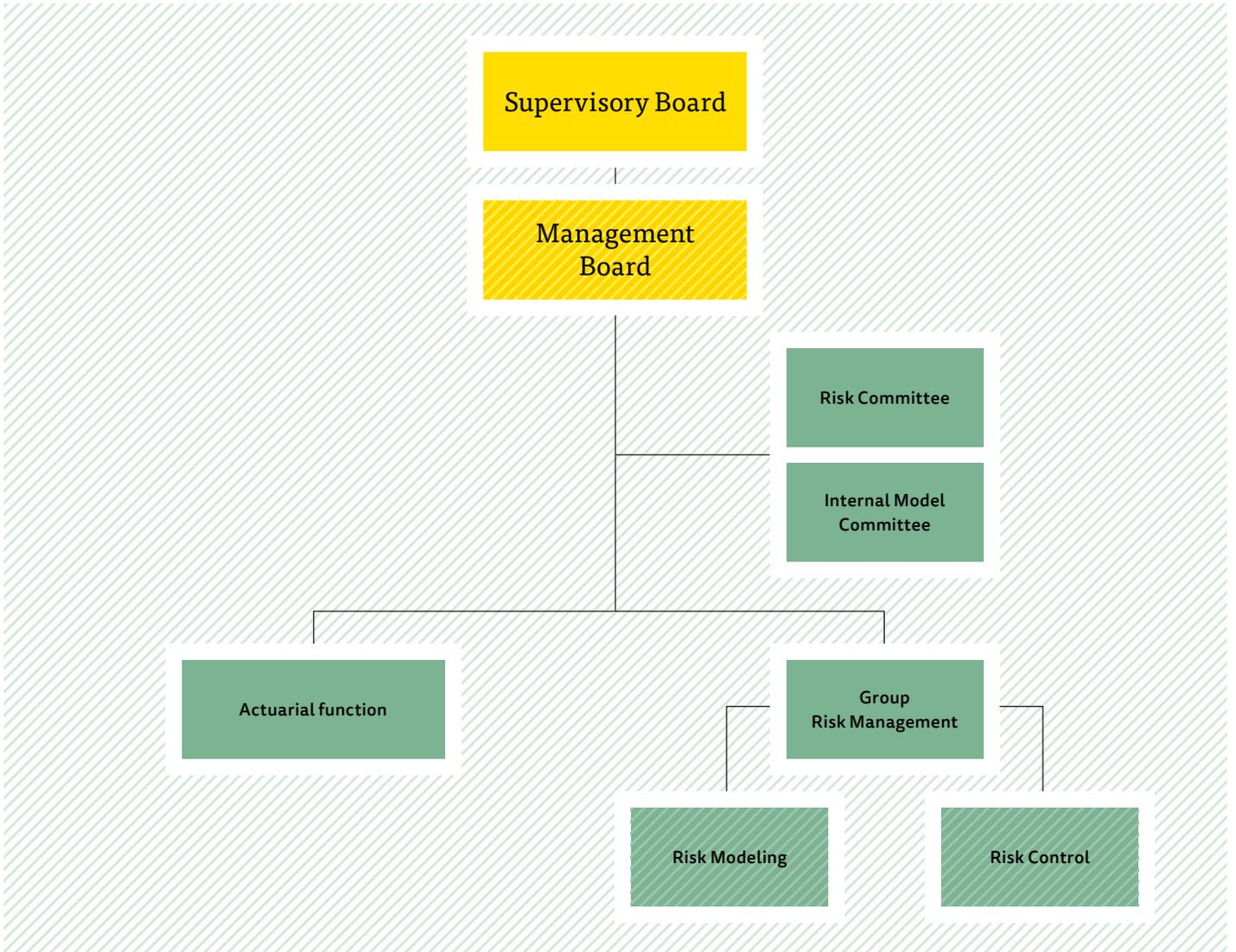
A regular validation process ensures that ARAG SE's partial internal model is always effective and its specifications are appropriate. Responsibility for validating the model lies with the Actuarial function. By assigning the task of model validation to this department, ARAG SE ensures the necessary independence of the validation process. Moreover, this organizational decision reflects the size and complexity of the Company.

Validation involves using qualitative and quantitative processes to check whether the results and forecasts of the partial internal model are sufficiently accurate. Both the mathematical and statistical methods used in the model and the governance processes relating to ARAG SE's partial internal model are verified. At the end of the annual validation cycle, the Actuarial function submits a comprehensive validation report to the ARAG SE Management Board, which makes sure that the partial internal model is suitable for measuring solvency in accordance with Solvency II and can be used as a basis for management decisions and corporate management.

Should it be necessary to modify the model as a result of the validation report or for other reasons, these changes are carried out using a process that is clearly defined in the model modification policy. Firstly, the Internal Model Committee classifies the intended change as either a major or a minor model modification. Model enhancements are not the responsibility of the Internal Model Committee. In such cases, a process to obtain new authorization from BaFin must be initiated. Major model modifications must be approved in writing by the Management Board and then submitted to BaFin for authorization. Minor model modifications are approved and initiated by the Risk Committee on the recommendation of the Internal Model Committee. All approved changes must be implemented without delay. BaFin is informed in writing on a quarterly basis of any minor model modifications that have been applied. The Actuarial function carries out an ad hoc validation process to review the implementation of major model modifications. BaFin is informed in good time if there are any plans for major model modifications. This ensures that the internal model is accurately tailored to the Company's circumstances at all times.

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## The Risk Committee's position within the organization



## B.4 Internal Control System

### Internal control system

The ARAG Group defines the internal control system (ICS) as follows: “The internal control system 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 has a consistent structure throughout the Group, ensuring that the connected systems and reports in the Group can be verified.

It 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. The ARAG Group pursues four main objectives with the ICS:

- Ensuring legal conformity: The ICS is designed to create and maintain compliance with an organizational framework that ensures that statutory and regulatory requirements are implemented.
- Helping to maintain the independence of the ARAG Group: The ICS is designed to help with identifying and reducing risks that may jeopardize the continued independence of the ARAG Group.
- Creating the framework for using the partial internal model in accordance with Solvency II: The ICS is designed to create the regulatory environment required for use of the partial internal model under Solvency II.
- Ensuring the effectiveness and profitability of business activities: Thanks to a functioning operational and organizational structure, the ICS contributes to effective and profitable business activities.

An organizational structure that is transparent and appropriate to the Company’s risk profile requires tasks and responsibilities to be clearly defined and delineated. Clear rules have to be imposed about who in the Company is responsible for tasks and who is responsible for signing off decisions. Above all, conflicts of interest between the establishment of risk exposures and the monitoring and control of these exposures must be avoided.

The Management Board occupies a special position within the organizational structure of the ICS because it is responsible for ensuring an orderly and effective system of governance and thus for ensuring that the Company’s risk management and its ICS are appropriate and effective. This means that the Management Board is directly responsible for the ARAG Group’s ICS. *Vis-à-vis* third parties, it is responsible for the appropriate specification of the ICS, i.e. its design, establishment, integrity, and monitoring as well as ongoing adjustments and refinements.

The Management Board has delegated the day-to-day running of the entire ICS to the responsible managers in the ARAG Group, i.e. the Senior Vice Presidents (in Germany) and Branch CEOs (internationally). The ARAG Group structures its ICS in accordance with the 'three lines of defense' model:

**First line of defense** The first line of defense is formed by all employees and managers in operational roles. Responsibility for risks and processes lies with the Senior Vice Presidents and Branch CEOs. If an organizational unit does not have a Senior Vice President, responsibility lies with the Vice President. The people in this first line are directly responsible for the risks and processes in their departments. In the risk control process, the risk managers are responsible for identifying and evaluating the risks in their area.

**Second line of defense** The monitoring of the business and central units is carried out by various interdisciplinary functions (Group Controlling Central Department, Group Legal/Compliance Central Department, Group Risk Management Central Department, and the Actuarial function) that are also part of the organizational structure of the ICS. They specify standards for the design and monitoring of controls and for the handling of risk.

**Third line of defense** The Group Audit Central Department conducts internal audits of the functions in the first and second lines of defense within the ARAG Group. The Group Audit Central Department is also the internal auditor for the Group companies that have contractually appointed it to this role.

As part of the ICS's operational structure, the processes relevant to the ICS are documented using a process and control system. This is made up of three elements: the process map (providing an overview of the overall operational structure), the process documentation, and the annual approval process. Processes are classified as being relevant to the ICS on the basis of the following criteria:

- Processes that, if not implemented, will jeopardize the achievement of the ARAG Group's targets (e.g. due to high financial losses, significant loss of reputation, sanctions imposed by the supervisory authority)
- Frequent/high-volume processes (particularly those tying up a large amount of employee capacity)
- Processes relating to a department's main tasks
- Processes that have to be documented by law.

## Compliance

Because of their intangible nature, insurance products require customers to place a great deal of trust in their insurance company. The leap of faith that customers have to make is based on the expectation that ARAG SE as an insurance company will comply with the contractual arrangements and legal requirements and, moreover, will measure itself by its own high standards. Customers also need to be able to rely on the Company having adequate and systematic management, control, and sanctioning mechanisms in place to ensure that it lives up to its value proposition. The ARAG Group's compliance management system therefore focuses on fulfilling these objectives.

At Group level, the compliance function is part of the Group Legal/Compliance Central Department and is the responsibility of the CEO. Although the Compliance Officer submits reports to the Management Board as a whole, he or she is directly and exclusively accountable to the CEO of ARAG SE.

The Risk Management, Compliance, and Internal Audit functions regularly share information with each other. This helps to ensure a risk-appropriate compliance structure, avoid duplication of work, and take account of the findings of the other functions when action is to be taken. Furthermore, the Compliance function is regularly audited by Internal Audit.

At Group level, it is also possible to establish a Compliance Steering Group to which the managers in the following areas belong:

- Company data protection officers
- Internal Audit
- IT Security
- Corporate Communications
- Risk Management.

This committee holds interdisciplinary discussions on compliance-relevant matters and coordinates management measures. If required, the steering group can be expanded to include other managers or reduced in size to make it more efficient.

## B.5 Internal Audit Function

The Group Audit function is an instrument of the Management Board, to which it is directly accountable and to which it reports. It is assigned to the Management Board member responsible for the Central Group Functions at ARAG SE, who is the board member to whom responsibility for Group Audit is assigned under the schedule of responsibilities. Group Audit is bound only by the instructions of the Management Board.

Group Audit assists the Management Board of ARAG SE with corporate management and helps it to fulfill its managerial and monitoring duties. Group Audit ensures that auditing activities are carried out professionally and in a manner appropriate to the risk situation, in relation to both the Company's targets and its operations.

Following the orders issued by the Management Board, Group Audit examines the operational and organizational structure as well as the ICS for all operating and business processes from a risk perspective.

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

To ensure that it is able to fulfill its role and responsibilities properly, Group Audit does not get involved in operational processes. It is not permitted to assign tasks to employees of Group Audit that would conflict with Group Audit's independence within the ARAG Group, nor are they 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.

To avoid conflicts of interest, ARAG Group Audit does not conduct any project-related audit procedures. Its involvement in projects is limited to an advisory role, in particular regarding the design of the ICS. Group Audit does not sign off the results of (sub)projects. This safeguards its independence and ensures it does not have any responsibility for the outcome of the projects in question.

## B.6 Actuarial Function

The Actuarial function is directly accountable to the member of the Management Board of ARAG SE responsible for Group Risk Management and Group Controlling. It acts independently of the units at ARAG SE with profit-and-loss responsibility. Its core tasks include ensuring that the methods, models, and assumptions used to calculate the technical provisions are appropriate. In addition, it ensures the appropriateness of ARAG SE's underwriting, contracting, and reinsurance policies. The Actuarial function has also been assigned responsibility for validating ARAG SE's partial internal model, so it plays an important part in implementing the risk management system.

To ensure that they are able to fulfill the tasks assigned to the Actuarial function adequately, the head of the Actuarial function and his or her employees must be able to communicate with all relevant employees at ARAG SE independently. They therefore have unrestricted access to the information that they need to complete their tasks and are notified of relevant matters promptly, including on an ad hoc basis if necessary. Each year, the Actuarial function submits an Actuarial function report to the Management Board containing information about the results of the work of the Actuarial function carried out over the year. Above all, this report provides evidence that the appropriateness of ARAG SE's technical provisions, underwriting and contracting policies, and reinsurance agreements is assured. Besides this general reporting channel, the head of the Actuarial function is also able to report directly to the Management Board and Supervisory Board of ARAG SE if necessary.

## B.7 Outsourcing

In accordance with section 7 no. 2 VAG, ARAG defines any kind of outsourcing as "an agreement in any form between an insurance company and a service provider, on the basis of which the service provider carries out a process, service, or task directly or by outsourcing it to another company that the insurance company would otherwise carry out itself; the service provider may or may not be subject to regulatory supervision". This includes services previously carried out by the insurance company itself and services that the insurance company could carry out itself.

Outsourcing in the regulatory sense therefore encompasses the outsourcing of functions and insurance activities by an insurance company to another entity.

Apart from the Management Board's primary tasks (in particular ensuring a proper system of governance and making strategic decisions), all activities can in principle be outsourced. Third parties can only be involved in these primary tasks in an advisory or support capacity.

Every outsourcing project must be assessed to establish whether it involves the outsourcing of a function or activity subject to the regulatory outsourcing requirements. Section 32 VAG specifies that this includes functions and insurance activities subject to enhanced requirements where the functions or insurance activities concerned are classified as important. If a project is to be classified as 'outsourcing', there must always be a relationship between the outsourced function or activity and the insurance business.

The outsourcing of a key function represents a special situation, however. In this case, the Management Board has to appoint an outsourcing officer for the outsourced function who is responsible for the proper performance of the key function by the service provider and has to meet the 'fit and proper' requirements because of his or her monitoring role. This applies regardless of whether the service provider is an external company or a Group company. Where outsourcing within the Group takes place, no less care is taken in respect of the outsourced projects and their monitoring and control, for example by the service provider's dedicated points of contact. Outsourcing within the Group may justify a more flexible approach in individual cases if this involves fewer risks than with outsourcing to an external company. Nevertheless, it is still essential that service activities in the individual Group companies are adequately separated from an organizational perspective. In general, ARAG SE ensures that outsourcing never has an adverse impact on the proper performance of the outsourced functions or insurance activities, on the Management Board's ability to manage and control them, or on the supervisory authority's ability to verify and control them. Moreover, the monitoring of the service provider by the supervisory authority is ensured at all times.

Apart from the outsourcing of some aspects of internal auditing in individual international branches, ARAG SE has not outsourced any other key functions to external companies. The four key functions of Compliance, Internal Audit, the Actuarial function, and Risk Management are carried out independently of each other within ARAG SE. No new outsourcing relationships, either within the Group or with third parties, were established in 2017 in respect of important functions or insurance activities.

## B.8 Any Other Information

ARAG SE has established an adequate system of governance based on clear business and risk strategies, an operational and organizational structure that is appropriate to its business activities and risk profile, and a culture in which risk is actively embraced.

The policies and related processes of the ICS at ARAG SE are continually reviewed and updated by the various departments involved – particularly the independent Internal Audit function – and are validated. This ensures that there is always appropriate communication between the Supervisory Board, Management Board, key functions, and other senior managers based on short, direct reporting channels and defined escalation procedures. The different hierarchy levels are supported in this by the use of cutting-edge technologies that deliver consistent and reliable data and make information available promptly in a manner that is suitable for the recipients.

ARAG SE believes that the effective interplay between governance, risk management, and compliance creates the necessary transparency for the supervisory authority, the auditors and, above all, its customers.

## C. Risk Profile

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In 2015, following a five-year preparatory phase, ARAG SE received authorization from BaFin for its partial internal model, on the basis of which it has been calculating its solvency capital requirement (SCR) since the introduction of Solvency II on January 1, 2016. ARAG SE is one of only a small number of German insurers that have successfully completed the certification process, which is a particularly good achievement given its size.

Using a partial internal model rather than the standard formula results in an appropriate assessment of the conservative risk position and enables ARAG SE to manage itself effectively in the context of the prescribed strategy. This strategy does not generally allow any risk to be transferred to special-purpose vehicles. Overall, the partial internal model provides greater protection for customers because risks are recognized adequately.

ARAG SE uses an internal model for the two biggest risk components: underwriting risk and market risk. The latter includes credit risk attaching to investments. These two risks were the principal risks over the entire period under review. They also include the main risk concentrations to which the Company is exposed.

Stress tests, backtesting, and scenario analysis for risk modules, sub-risks, and individual parameters are conducted as part of model validation, the ORSA process, and other regular analyses. The internally stipulated coverage ratio of 150 percent means that customers are protected by a considerably larger risk buffer than required by the supervisory authority. Various influencing factors were stress-tested and the impact on the coverage ratio in different scenarios was analyzed. Because of the Company's very good capital adequacy, no relevant scenarios were identified that would be a threat to the protection of customers or in terms of the Company's exposure to risk. The findings of the various analyses are discussed in detail with the relevant risk managers and the Management Board and possible solutions for reducing or mitigating risk are drawn up.

The solvency requirements used in the following chapters should be considered in the context of article 297 (2) (a) of the Delegated Regulation. All quantitative disclosures relate to the figures in the quantitative reporting formats set out in the Appendix.

## C.1 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 the following risk categories:

- 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 potential accumulation losses 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.

To minimize risk, the Company uses reinsurance agreements in legal insurance segments with a particularly high exposure.

Despite the use of the aforementioned risk mitigation techniques, a concentration of risk could arise if individual losses could potentially materialize simultaneously. However, a limit system is used to make sure that this risk is kept to a level that the Company can bear.

Various stress tests and sensitivity analyses were carried out in the reporting period. These tests and analyses included measurements of the impact from changes of up to 20 percent in the premiums, claims incurred, and costs. In these extreme scenarios, ARAG SE's coverage ratios did not fall below a minimum of 236 percent, which would still represent a significant risk buffer for customers based on the Company's very good level of capital adequacy.

As of December 31, 2017, the solvency capital requirement for underwriting risk amounted to €158,005 thousand, which equated to a year-on-year decline of €20,061 thousand, or 11 percent, compared with the prior-year figure of €178,066 thousand. The main risk drivers were premium and reserve risk.

There were no significant changes in the risk assessment methodology in the period under review.

## C.2 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
- Equity risk: changes in the level or volatility of the market prices of equities
- 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
- Currency risk: changes in the level or volatility of exchange rates

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, 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 within institutional funds 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.

Potential risk concentrations in the investment portfolio are countered by applying a policy of diversification, which is integral to the prudent person principle. The system of limits also restricts an excessive concentration of market risk. Various stress tests and sensitivity analyses were carried out in the reporting period. These tests and analyses included measurement of the potential impact from changes of up to 210 basis points in individual market parameters such as real estate, equities, and spreads on government and corporate bonds. In these extreme scenarios, ARAG SE's coverage ratios fell to a minimum of 242 percent, which would still be sufficient and continue to represent a significant risk buffer for customers based on the Company's very good level of capital adequacy.

As of December 31, 2017, the solvency capital requirement for market risk was €313,983 thousand, which equated to a decline of €66,889 thousand, or 18 percent, compared with the figure of €380,872 thousand as of December 31, 2016, the main risk drivers being equity risk, equity investment risk, and spread risk. This year-on-year fall in market risk was primarily attributable to a decrease in equity investment risk, which diminished substantially with the disposal of ARAG Lebensversicherungs-AG. Based on a recommendation from the Actuarial function, no calculation of concentration risk was carried out in the period under review as such risk was not deemed to be material. The extent to which concentration risk is material or not will continue to be reviewed on an ongoing basis and the approach will be adjusted, if appropriate. Otherwise, there were no significant changes in the risk assessment methodology in the period under review.

### C.3 Credit 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 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. Receivables from policyholders are managed by means of an automated reminder and dunning process.

The solvency capital requirement for counterparty default risk amounted to €13,638 thousand as of December 31, 2017, which equated to a year-on-year rise of €493 thousand (4 percent). There were no significant changes in the risk assessment methodology in the period under review.

## C.4 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 capital 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. If it becomes apparent that selling securities is also becoming more difficult, the Company responds by increasing the liquidity that it holds as a safety buffer. Further protection is provided by the current investment policy, which stipulates diversification across a broad range of security types and issuers.

The expected profits included in future premiums represent a very illiquid component of basic own funds. These profits are therefore associated with a potential liquidity risk. If the expected profits contained in future premiums are not factored into basic own funds, the resulting liquidity risk is classified as very low because of the significant excess cover. The expected profits included in future premiums amount to €70,983 thousand.

## C.5 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. 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 and their actual impact on the income statement.

Specific measures are agreed upon and carried out at operational level in order to reduce the identified risks. The following strategies for dealing with a risk are possible:

- Accept – no measures to reduce the effects are possible or considered necessary.
- Mitigate – the effects are mitigated by taking suitable measures.
- Transfer – the effects are transferred to another risk carrier, e.g. by means of outsourcing or reinsurance.
- Avoid – measures are taken to avoid the risk, even as far as not carrying out the activities that give rise to the risk.

With regard to cyber risk, these strategies 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. The strategy put in place is documented and its implementation is monitored on an ongoing basis. The solvency capital requirement for operational risk amounted to €28,914 thousand as of December 31, 2017, which equated to a year-on-year fall of €637 thousand (2 percent). There were no significant changes in the risk assessment methodology in the period under review.

## C.6 Other Material Risks

The Company is not exposed to any other material risks.

## C.7 Any Other Information

The preceding chapters contain all of the important information about the risk profile.

## D. Valuation for Solvency Purposes

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The explanation below of each balance sheet line item's valuation methods and their differences starts with a description of their valuation (gross) under the German Commercial Code (HGB)\* followed by a description of their valuation for solvency purposes (Solvency II, SII) and then an explanation of any material differences. The SII figures are also compared with the equivalent prior-year figures.

Other than in the case of the valuation of investments in affiliated companies and in equity investments, there were no changes in the reporting period in the valuation bases used on the Solvency II balance sheet for the individual assets and liabilities described below.

All quantitative disclosures relate to the figures in the quantitative reporting formats set out in the Appendix. Figures are presented in thousands of euros.

\* The breakdown of the line items corresponds to that in the SII structure.

## D.1 Assets

### Comparison of assets on the HGB balance sheet and Solvency II balance sheet

#### Assets as of December 31, 2017

(€'000)

<b>Intangible assets</b>
<b>Deferred tax assets</b>
<b>Pension benefit surplus</b>
<b>Property, plant &amp; equipment held for own use</b>
<b>Investments (other than assets held for index-linked and unit-linked contracts)</b>
Property (other than for own use)
Holdings in related undertakings, including participations
Equities
Equities – listed
Equities – unlisted
Bonds
Government bonds
Corporate bonds
Structured notes
Collateralized securities
Collective investment undertakings
Derivatives
Deposits other than cash equivalents
Other investments
Carried forward:

	Solvency II as of Dec. 31, 2017	HGB as of Dec. 31, 2017	Difference as of Dec. 31, 2017	Solvency II as of Dec. 31, 2016	Solvency II year-on-year change
	0	7,658	-7,658	0	0
	72,806	0	72,806	75,812	-3,006
	0	0	0	0	0
	54,049	45,317	8,732	59,885	-5,836
	32,856	23,271	9,585	28,201	4,655
	817,923	329,498	488,425	986,173	-168,250
	243	243	0	154	90
	781	719	61	781	0
	<b>851,803</b>	<b>353,732</b>	<b>498,071</b>	<b>1,015,308</b>	<b>-163,505</b>
	208,570	196,560	12,009	205,717	2,852
	622,966	593,635	29,331	529,024	93,941
	7,310	5,504	1,806	6,647	663
	1,084	1,027	57	1,117	-33
	<b>839,929</b>	<b>796,726</b>	<b>43,203</b>	<b>742,506</b>	<b>97,424</b>
	638,901	616,660	22,241	644,496	-5,595
	0	0	0	0	0
	57,969	57,969	0	98,581	-40,612
	7,453	4,536	2,917	7,486	-33
	<b>2,396,055</b>	<b>1,829,623</b>	<b>566,432</b>	<b>2,508,377</b>	<b>-112,321</b>
	<b>2,522,910</b>	<b>1,882,598</b>	<b>640,312</b>	<b>2,644,074</b>	<b>-121,163</b>

## Comparison of assets on the HGB balance sheet and Solvency II balance sheet

### Assets as of December 31, 2017

(€'000)

Brought forward:

#### Assets held for index-linked and unit-linked contracts

##### Loans and mortgages

Loans on policies

Loans and mortgages to individuals

Other loans and mortgages

##### Reinsurance recoverables from

Non-life and health similar to non-life

Non-life excluding health

Health similar to non-life

Life and health similar to life, excluding health and index-linked and unit-linked

Health similar to life

Life excluding health and index-linked and unit-linked

Life index-linked and unit-linked

##### Receivables

Deposits to cedants

Insurance and intermediaries receivables

Reinsurance receivables

Receivables (trade, not insurance)

##### Other assets

Own shares (held directly)

Amounts due in respect of own fund items or initial fund called up but not yet paid in

Cash and cash equivalents

Any other assets, not elsewhere shown

#### Total assets

	Solvency II as of Dec. 31, 2017	HGB as of Dec. 31, 2017	Difference as of Dec. 31, 2017	Solvency II as of Dec. 31, 2016	Solvency II year-on-year change
	2,522,910	1,882,598	640,312	2,644,074	- 121,163
	0	0	0	0	0
	0	0	0	0	0
	79	79	0	150	- 71
	9,180	9,180	0	5,915	3,265
	<b>9,259</b>	<b>9,259</b>	<b>0</b>	<b>6,065</b>	<b>3,194</b>
	699	3,985	- 3,287	270	429
	0	0	0	0	0
	<b>699</b>	<b>3,985</b>	<b>- 3,287</b>	<b>270</b>	<b>429</b>
	0	0	0	0	0
	0	0	0	0	0
	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
	0	0	0	0	0
	<b>699</b>	<b>3,985</b>	<b>- 3,287</b>	<b>270</b>	<b>429</b>
	49,677	49,677	0	44,389	5,288
	45,442	45,442	0	45,830	- 388
	46,740	46,740	0	44,836	1,904
	31,357	31,357	0	48,590	- 17,233
	<b>173,217</b>	<b>173,217</b>	<b>0</b>	<b>183,644</b>	<b>- 10,427</b>
	0	0	0	0	0
	0	0	0	0	0
	58,303	58,303	0	67,913	- 9,610
	2,739	2,739	0	2,197	542
	<b>61,042</b>	<b>61,042</b>	<b>0</b>	<b>70,110</b>	<b>- 9,068</b>
	<b>2,767,127</b>	<b>2,130,102</b>	<b>637,025</b>	<b>2,904,163</b>	<b>- 137,036</b>

**Intangible assets**

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total intangible assets</b>	<b>0</b>	<b>7,658</b>	<b>-7,658</b>	<b>0</b>	<b>0</b>

Intangible assets are only included on the balance sheet if they were purchased. Their cost is amortized in accordance with their estimated useful life using the straight-line method. If the fair value is permanently below this residual value, the lower of the two values is recognized.

As in 2016, intangible assets are not recognized on the Solvency II balance sheet because market valuation is too uncertain.

Due to intangible assets not being included for solvency purposes, the difference compared with the figure on the HGB balance sheet amounts to €7,658 thousand.

**Deferred tax assets**

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total deferred tax assets</b>	<b>72,806</b>	<b>0</b>	<b>72,806</b>	<b>75,812</b>	<b>-3,006</b>

If differences arise between the carrying amounts on the Solvency II balance sheet and those in the tax base and these differences are expected to reverse in subsequent years, deferred taxes are recognized on the Solvency II balance sheet in respect of these differences using separate entity-specific tax rates determined according to the country in which the registered office of the permanent establishment/branch 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 will only reverse in the event of any liquidation. For the purpose of recognition on the Solvency II balance sheet, the effects of the reversal of the differences between the Solvency II balance sheet and the tax base are reviewed in terms of their impact on the basis of tax assessment. Differences that would not be accompanied by sufficient taxable income at the time of reversal or would not be offset by countervailing effects in deferred taxes are not recognized. A simplified tax planning process on the basis of the multi-year planning is used for the evaluation. Loss carryforwards are not included when determining deferred taxes. Future tax expense resulting from the reversal effects is always recognized. Deferred taxes from tax group subsidiaries (companies controlled by the parent company and/or with which a profit-and-loss transfer agreement has been concluded) are recognized by the parent company because the income of the tax group is aggregated for tax purposes and taxed overall at the level of the parent company. Of this income, €23,800 thousand was transferred from subsidiaries.

The deferred tax assets on the Solvency II balance sheet are deemed not to be impaired. This is because the deferred tax liabilities are dominant on the Solvency II balance sheet and an analysis of the timing of the reversal effects proves that the time until reversal of the deferred tax expense is shorter than the time until reversal of the deferred tax benefit. The expense thus materializes earlier than the benefit. The deferred tax assets largely arise because defined benefit obligations and other obligations to employees in connection with pre-retirement part-time employment, early retirement, and long-service awards are valued at a higher level under regulatory requirements than under tax regulations.

The calculation of deferred taxes takes into account applicable tax legislation and tax rates in those countries in which ARAG SE maintains permanent establishments/branches. The tax rates are as follows:

• ARAG SE headquarters	31.23 percent
• Austria Branch	25.00 percent
• Belgium Branch	33.99 percent
• Greece Branch	29.00 percent
• Italy Branch	30.82 percent
• Netherlands Branch	25.00 percent
• Portugal Branch	21.00 percent
• Slovenia Branch	19.00 percent
• Spain Branch	25.00 percent

There were no changes in the recognition and valuation methods compared with the previous year.

### Pension benefit surplus

There was no pension benefit surplus at ARAG SE in the year under review.

### Property, plant & equipment held for own use

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total property, plant &amp; equipment held for own use</b>	<b>54,049</b>	<b>45,317</b>	<b>8,732</b>	<b>59,885</b>	<b>-5,836</b>

Equipment is recognized at cost on the balance sheet and subsequently depreciated using the straight-line method over the standard operating useful life.

The treatment of equipment for solvency purposes is no different to its treatment under the HGB.

Because the valuation methods are identical, there are no valuation differences.

Real estate (property) held for own use is valued at cost less depreciation. If its value is permanently impaired, it is written down to the lower of fair value or depreciated cost. If the reason for the impairment ceases to apply, the write-down is reversed to the depreciated value of the asset. Land and buildings are categorized as being held for own use or rented out to third parties according to actual usage. For this purpose, a uniform carrying amount is recognized on a pro rata basis. Fair values are used for Solvency II purposes. The year-on-year decrease in the Solvency II carrying amount of €5,836 thousand was attributable to the decline in the fair values of the real estate. There were no changes in the recognition and valuation methods compared with the previous year.

### Property (other than for own use)

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total property (other than for own use)</b>	<b>32,856</b>	<b>23,271</b>	<b>9,585</b>	<b>28,201</b>	<b>4,655</b>

On the Solvency II balance sheet, the value of property (other than for own use) is based on prevailing standard land values. The value of the buildings is calculated using the income capitalization approach. This method discounts the expected future rental income less the likely management costs to the balance sheet date. The overall value is the sum of the value of the land and the value of the buildings. Land and buildings are categorized as being held for own use or rented out to third parties in the same way as for the HGB balance sheet.

Differences arise between the Solvency II balance sheet and the HGB financial statements because the historical cost convention is applied in the valuation under the HGB, whereas the higher unrealized fair values are recognized on the Solvency II balance sheet. As of December 31, 2017, unrealized valuation reserves amounted to €9,585 thousand. The year-on-year increase in the Solvency II carrying amount of €4,655 thousand was attributable to the disposal of a plot of land and a countervailing increase in the fair values of the real estate. There were no changes in the recognition and valuation methods compared with the previous year.

**Holdings in related undertakings, including participations**

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total holdings in related undertakings, including participations</b>	<b>817,923</b>	<b>329,498</b>	<b>488,425</b>	<b>986,173</b>	<b>-168,250</b>

Holdings in related undertakings, including participations are valued at cost, in some cases reduced by write-downs to fair value and by specific equity investment risk arising on the equity investments. Write-downs are reversed to no more than the historical cost if the reason for recognizing them ceases to apply. The fair value is determined using an income capitalization approach based on a planning horizon of three years.

The method used to value subsidiaries and equity investments for solvency purposes depends on their type. Insurance subsidiaries, intermediate holding companies, and insurance operating companies are valued on the basis of the pro rata excess of the assets over the liabilities of the subsidiary as recognized on its Solvency II balance sheet. The valuation of the assets and liabilities on a subsidiary's Solvency II balance sheet is based on the valuation rules for solvency purposes. At the first valuation level, other subsidiaries are valued at market price. If no market prices are available, they are recognized at the second valuation level on the basis of their pro rata equity derived from modified financial statements in which special assets and liabilities are valued in accordance with the principles of valuation for solvency purposes and the International Financial Reporting Standards (IFRS).

The differences between the values recognized in the HGB financial statements and those recognized on the Solvency II balance sheet arise in qualitative terms from the entirely different valuation methods used for insurance subsidiaries. Under the HGB, the values are limited to the historical costs, which in some cases date back a long way. The total value on the Solvency II balance sheet as of December 31, 2017 was €488,425 thousand higher than the total value on the HGB balance sheet. The year-on-year decrease in the Solvency II carrying amount of €168,250 thousand was mainly attributable to the net effect from the disposal of one affiliated company and the addition of a controlling interest in another.

## Equities

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Equities – listed	243	243	0	154	90
Equities – unlisted	781	719	61	781	0
<b>Total equities</b>	<b>1,024</b>	<b>963</b>	<b>61</b>	<b>934</b>	<b>90</b>

Equities that, overall, are not intended for permanent use in insurance operations are valued at the lower of their cost or quoted market price or market value as of the balance sheet date. This applies even if the quoted market price or market value is only temporarily lower than the cost.

For solvency purposes, equities are valued at their quoted market price or market value. If this price/value is not available, the value is estimated using a valuation model. If the necessary information for an interest-rate premium on the security or on the issuer is not available, the premium is determined – where available – on the basis of the investment's credit rating; otherwise, the credit rating of the issuer or the sector is used.

The differences in the valuation rules resulted in a valuation difference of €61 thousand for unlisted equities as of December 31, 2017. The difference of €90 thousand between the latest Solvency II value and the equivalent value as of December 31, 2016 was entirely attributable to changes in market value. There were no changes in the recognition and valuation methods compared with the previous year.

## Bonds

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Government bonds	208,570	196,560	12,009	205,717	2,852
Corporate bonds	622,966	593,635	29,331	529,024	93,941
Structured notes	7,310	5,504	1,806	6,647	663
Collateralized securities	1,084	1,027	57	1,117	-33
<b>Total bonds</b>	<b>839,929</b>	<b>796,726</b>	<b>43,203</b>	<b>742,506</b>	<b>97,424</b>

Bonds that, overall, are not intended for permanent use in insurance operations are valued under the HGB at the lower of their cost or quoted market price or market value as of the balance sheet date. This applies even if the quoted market price or market value is only temporarily lower than the cost.

Registered bonds are accounted for at their nominal or redemption amount. Discounts are deferred using the straight-line method. Premiums are treated as a prepaid expense and recognized in income using the straight-line method over the term to maturity.

The economic values of interest-bearing financial instruments are calculated for solvency purposes at the quoted market price or market value that contains the accrued interest income as of the valuation date. Premiums and discounts are not recognized separately.

Compared with recognition under the HGB, the valuation of fixed-income securities in accordance with the rules described above has resulted in valuation reserves of €43,203 thousand that have not yet been realized. The year-on-year increase in the Solvency II carrying amount of €97,424 thousand was attributable to a combination of portfolio growth and a countervailing fall in fair values. There were no changes in the recognition and valuation methods compared with the previous year.

### Collective investment undertakings

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Equities	193,893	182,228	11,665	177,210	16,683
Bonds	406,072	396,170	9,901	425,384	-19,312
Other	38,936	38,261	675	41,902	-2,966
<b>Total collective investment undertakings</b>	<b>638,901</b>	<b>616,660</b>	<b>22,241</b>	<b>644,496</b>	<b>-5,595</b>

Collective investment undertakings that are not intended for permanent use in insurance operations are valued under the HGB at the lower of their cost or quoted market price or market value as of the balance sheet date. This applies even if the quoted market price or market value falls below the cost only for a short time. Write-downs are reversed to no more than the cost if the reason for recognizing them ceases to apply.

ARAG SE made use of the option to select the discretionary principle of lower of cost or market value for those institutional investment fund shares/units that the Management Board intends to use permanently as part of the working capital of the insurance business. These are valued at cost, even if their quoted market price or market value decreases temporarily. They are not written down to fair value until they are permanently impaired. If the reason for the write-down ceases to apply, it is reversed to no more than the cost. For solvency purposes, the redemption price determined by the investment management company for the investment fund units/shares is used to determine the economic value. This value is not restricted to the cost.

In accordance with Delegated Regulation (EU) No. 2015/2450, Annex II, collective investment undertakings in which the stake held is at least 20 percent are reported under investment fund shares/units and not under holdings in related undertakings, including participations.

The restriction of the valuation under HGB rules as a result of the historical cost convention and the realization principle mean that the valuation for solvency purposes was €22,241 thousand higher as of December 31, 2017. The year-on-year decrease in the Solvency II carrying amount of €5,595 thousand was attributable to a combination of portfolio contraction and a countervailing rise in fair values. There were no changes in the recognition and valuation methods compared with the previous year.

### Derivatives

ARAG SE did not have any direct investments in derivatives as of the balance sheet date or as of the prior-year reporting date.

### Deposits other than cash equivalents

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total deposits other than cash equivalents</b>	57,969	57,969	0	98,581	-40,612

Deposits other than cash equivalents are recognized at their nominal amount. Taking account of the materiality principle, the nominal amount is also used as the economic value.

Because of the identical valuation methods, the value under the HGB and the value for solvency purposes are the same. The Solvency II carrying amount fell by €40,612 thousand year on year because balances were reduced. There were no changes in the recognition and valuation methods compared with the previous year.

### Other investments

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total other investments</b>	7,453	4,536	2,917	7,486	-33

Other investments are valued at cost, in some cases reduced by write-downs to the lower fair value. The fair value is determined by the net asset value (NAV) published by the investment management company.

For solvency purposes, the NAV reported by the private equity company is recognized as the economic value, even if it is higher than the cost.

As a result of unrealized valuation reserves, the value for solvency purposes as of December 31, 2017 was €2,917 thousand higher than the HGB value. The year-on-year decrease in the Solvency II carrying amount of €33 thousand was attributable to a combination of a contraction in the portfolio of private equity and infrastructure investments and a countervailing rise in fair values. There were no changes in the recognition and valuation methods compared with the previous year.

### Assets held for index-linked and unit-linked contracts

There were no assets held for index-linked and unit-linked contracts to be recognized at the end of 2017.

### Loans and mortgages

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Loans on policies	0	0	0	0	0
Loans and mortgages to individuals	79	79	0	150	-71
Other loans and mortgages	9,180	9,180	0	5,915	3,265
<b>Total loans and mortgages</b>	<b>9,259</b>	<b>9,259</b>	<b>0</b>	<b>6,065</b>	<b>3,194</b>

Loans and mortgages in the form of promissory notes, loans and receivables secured by mortgages or land charges, loans, and sundry lending items are recognized at cost unless permanently impaired. In this case, they are written down to their fair value. If the reasons for the write-down cease to apply, it is reversed to no more than the cost.

For solvency purposes, the economic value of loans and mortgages maturing within twelve months is based on the nominal amount. The economic value of those maturing in more than twelve months is determined by applying a present value method. Regardless of the term of the receivable, the counterparty's default risk is determined using an internal credit rating process based on historical default rates and is reflected in the valuation accordingly. The year-on-year increase in the Solvency II carrying amount of €3,194 thousand was mainly attributable to the rise in volume. In contrast to the approach in 2016, no further present value calculations were carried out in the year under review for reasons of materiality. Instead, HGB carrying amounts were also used for Solvency II purposes.

**Reinsurance recoverables**

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Non-life and health similar to non-life	699	3,985	- 3,287	270	429
<b>Total reinsurance recoverables</b>	<b>699</b>	<b>3,985</b>	<b>- 3,287</b>	<b>270</b>	<b>429</b>

To calculate the reinsurance recoverables, the reinsurers' share of the unearned premiums is determined in accordance with the contractual agreements.

Reinsurance in the form of an excess-of-loss treaty has been taken out in connection with special criminal-case legal insurance and financial-loss legal insurance in Germany. ARAG SE also has reinsurance to cover accumulation loss arising from the travel insurance it provides in the Spanish market; this is also in the form of an excess-of-loss treaty. The bulk of travel accident and travel liability risks in connection with insurance provided in Spain are re-insured through quota-share reinsurance treaties.

On the HGB balance sheet, the reinsurers' share of technical provisions is deducted from the provision for unearned premiums and the provision for outstanding claims. The reinsurers' share of the unearned premiums is determined in accordance with the contractual agreements. The proportions of the provision for outstanding claims relating to outward reinsurance business are calculated in accordance with the stipulations in the reinsurance treaties.

On the economic balance sheet, the reinsurers' shares are aggregated. To determine the economic value, the reinsurers' pro rata share of the technical provisions is calculated using the reinsurers' best estimate in accordance with the underlying treaty. The reinsurers' share is determined on an individual claim basis in accordance with the contractual terms.

Applying the aforementioned valuation methods, the carrying amount on the Solvency II balance sheet as of December 31, 2017 was €3,287 thousand lower than the HGB carrying amount. The year-on-year increase in the Solvency II carrying amount of €429 thousand was attributable to the continuation of business operations. There were no changes to valuation methods in the year under review.

## Receivables

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Deposits to cedants	49,677	49,677	0	44,389	5,288
Insurance and intermediaries receivables	45,442	45,442	0	45,830	- 388
Reinsurance receivables	46,740	46,740	0	44,836	1,904
Receivables (trade, not insurance)	31,357	31,357	0	48,590	- 17,233
<b>Total receivables</b>	<b>173,217</b>	<b>173,217</b>	<b>0</b>	<b>183,644</b>	<b>- 10,427</b>

Deposits to cedants are recognized at their nominal amount, which equates to their cost.

The economic value of those maturing within twelve months is based on the nominal amount. The economic value of those maturing in more than twelve months is determined by applying a present value method. Regardless of the term of the receivable, the counterparty's default risk is determined using an internal credit rating process based on historical default rates and is reflected in the valuation accordingly.

There are no valuation differences due to use of the nominal amount as the economic value. There were no changes in the recognition and valuation methods compared with the previous year.

Insurance and intermediaries 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 economic value of those maturing within twelve months is based on the nominal amount. The economic value of those maturing in more than twelve months is determined by applying a present value method. Regardless of the term of the receivable, the counterparty's default risk is recognized in accordance with the method used for specific and general allowances under the HGB.

There are no valuation differences due to use of the nominal amount as the economic value.

Reinsurance receivables are recognized at the nominal amount of the outstanding balances. In the event of actual default risk relating to rating downgrades, specific allowances are recognized in the amount that is no longer likely to be recovered.

The economic value of those maturing within twelve months is based on the nominal amount. The economic value of those maturing in more than twelve months is determined by applying a present value method. Regardless of the term of the receivable, the counterparty's default risk is recognized in accordance with the method used for specific allowances under the HGB.

There are no valuation differences due to use of the nominal amount as the economic value.

Receivables (trade, not insurance) are generally recognized at their nominal amount. In the event of actual default risk relating to rating downgrades, specific allowances are recognized in the amount that is no longer likely to be recovered.

The economic value of those maturing within twelve months is based on the nominal amount. The economic value of those maturing in more than twelve months is determined by applying a present value method. Regardless of the term of the receivable, the counterparty's default risk is recognized in accordance with the method used for specific allowances under the HGB.

There are no valuation differences due to use of the nominal amounts as the economic value. There were no changes in the recognition and valuation methods compared with the previous year.

The year-on-year decrease in the Solvency II carrying amount of €10,427 thousand was attributable to ongoing business operations.

#### **Own shares (held directly)**

As of the reporting date, there were no own shares (held directly) to be recognized.

#### **Amounts due in respect of own fund items or initial fund called up but not yet paid in**

Likewise, there was nothing to report as of December 31, 2017 for amounts due in respect of own fund items or initial fund called up but not yet paid in.

**Cash and cash equivalents**

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total cash and cash equivalents</b>	<b>58,303</b>	<b>58,303</b>	<b>0</b>	<b>67,913</b>	<b>-9,610</b>

Cash and cash equivalents are recognized at their nominal amount, which equates to their cost.

There are no valuation differences due to use of the nominal amount as the economic value. The year-on-year decrease in the Solvency II carrying amount of €9,610 thousand was attributable to the reduction in balances. There were no changes in the recognition and valuation methods compared with the previous year.

**Any other assets, not elsewhere shown**

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total of any other assets, not elsewhere shown</b>	<b>2,739</b>	<b>2,739</b>	<b>0</b>	<b>2,197</b>	<b>542</b>

Any other assets, not elsewhere shown are recognized at their nominal amount, which equates to their cost. Long-term tax assets are discounted to present value using a discount rate appropriate to the maturity involved.

There are no valuation differences due to use of the nominal amount as the economic value. The year-on-year increase in the Solvency II carrying amount of €542 thousand was attributable to year-on-year inventory differences. There were no changes in the recognition and valuation methods compared with the previous year.

Please refer to section A.4 for disclosures relating to leases.

## D.2 Technical Provisions

### Comparison of technical provisions on the HGB balance sheet and Solvency II balance sheet

#### Technical provisions as of December 31, 2017

(€'000)

##### Technical provisions – non-life

Technical provisions – non-life (excluding health)

Technical provisions calculated as a whole

Best estimate

Risk margin

Technical provisions – health (similar to non-life)

Technical provisions calculated as a whole

Best estimate

Risk margin

##### Technical provisions – life (excluding index-linked and unit-linked)

Technical provisions – health (similar to life)

Technical provisions calculated as a whole

Best estimate

Risk margin

Technical provisions – life (excluding health and index-linked and unit-linked)

Technical provisions calculated as a whole

Best estimate

Risk margin

##### Technical provisions – index-linked and unit-linked

Technical provisions calculated as a whole

Best estimate

Risk margin

##### Other technical provisions

##### Total provisions



### Technical provisions

On the HGB balance sheet, the technical provisions include unearned premiums, the provision for outstanding claims, the equalization provision and similar provisions, and miscellaneous technical provisions.

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 (international units of the Company) 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 is recognized for obligations arising on claims that had occurred by the end of the reporting year and for the associated claim settlement expenses, unless they have already been settled. Recourse claims, excess proceeds, and claims under loss sharing agreements are deducted from the claims provision. These are receivables that arose due to compensation paid as a result of recourse rights or that are due from other insurers on the basis of loss sharing agreements.

The provisions for outstanding claims are divided into provisions for direct insurance business and provisions for inward reinsurance business.

### Provisions for direct insurance business

Applying the prudence principle, this provision is measured in such a way that all expected claim payments for reported claims and claims incurred but not reported, including the claim settlement costs, are covered. Run-off losses are to be avoided because these have an adverse impact on customers in future financial years.

The provision for outstanding claims is calculated separately for each insurance segment. The provision for outstanding claims is made up of the following partial provisions for each claim event year:

- Provision for claims occurring in the reporting year (claims reported for the reporting year)
- Provision for claims occurring in previous years (claims reported for previous years)
- Provision for claim settlement costs.

The claims in each year are valued separately.

a) Partial provisions for external claim costs relating to claims reported for the reporting year: This provision is the difference between the claims incurred in the reporting year and the claim payments already made in the reporting year. The claims incurred in the reporting year are calculated on the basis of the observed average values of claims for the claim event year that was two years prior to the reporting year, taking account of payments already made and the payments expected to be made in the future.

The quantitative data for the claims reported for the reporting year is taken from the claims inventory. The size of the claims incurred but not reported by the end of the reporting year has to be estimated using the late claims statistics for the ten event years prior to the reporting year.

b) Partial provisions for external claim costs relating to claims reported for previous years: The provision brought forward from the previous year is utilized first for the claim payments made in the reporting year. The amount of the late claims that had previously not been reported is reclassified from the partial provision for claims incurred but not reported to the partial provision for late claims that had previously not been reported.

Each year, a claims inventory is drawn up for the year that was six years prior to the reporting year and for all earlier years. This involves examining each individual claim record and recognizing a reserve. The results of the individual valuations are recorded in the claims register.

c) Partial provision for external claim costs relating to claims incurred in previous years but not reported: The number and value of the claims incurred in previous years but not yet reported have to be estimated. The quantity, the time of reporting, and the amount of the claim payments can only be estimated using past experience.

d) Partial provision for claim settlement costs: A special partial provision is recognized for internal and external expenses incurred after the balance sheet date in connection with settling claims. Claim settlement involves investigating a claim and the work involved in dealing with the claim.

Claim settlement costs comprise both direct and indirect costs. Indirect costs are the cost of inhouse claims departments and inhouse attorneys, e.g. in the Netherlands, and pro rata expenses for central departments.

### **Provisions for inward reinsurance business**

The provision is recognized in accordance with the information provided by the ceding insurer. If there are indications that the information is incomplete or incorrect, ARAG SE calculates the provision itself or estimates it professionally and conscientiously. It has its own statistical observation instruments that it can use to make such estimates.

The results from the group-based and individual valuations are reviewed on a portfolio basis using actuarial methods.

The equalization provision for direct insurance business and inward reinsurance business is recognized as additional actuarial reserves that can be used to offset fluctuations in the course of business. 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 legal requirements for valuation are set out in detail in the annex to section 29 of the German Regulation on the Accounting of Insurance Undertakings (RechVersV).

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.

The technical provisions on the Solvency II balance sheet are determined by the Group Risk Management Central Department. The individual components of the technical provisions are:

- Claims provision (including provision for external claim payments and internal claim settlement costs)
- Premiums provision
- Risk margin
- Amounts recoverable from reinsurance recognized as asset items on the Solvency II balance sheet.

The claims provisions are calculated for each previously defined homogeneous risk group of ARAG SE. They contain expected claim payments and claim settlement costs that are necessary for the settlement of claims already incurred. The claims reserve is valued using the standard actuarial reserving methods used in the market: the chain-ladder method, the additive method based on accident-year-independent growth of the claims ratio (AUSQZ), and the Bornhuetter-Ferguson method. Alternative reserving methods may be used in exceptional cases, for example if all three of these methods produce implausible results. The New York method is used to value the claim settlement provision.

The premiums provisions are made up of the provision for premiums written but not yet earned and the expected profit or loss from in-force policies. The provision for premiums written but not yet earned is recognized in the amount of the present values of the expected claim payments and costs relating to the relevant policies. The expected profit or loss is determined for the outstanding premium income from in-force policies (installment payments and premiums from multi-year policies). Results from the internal model are used for the valuation of these two line items on the Solvency II balance sheet.

The risk margin is calculated using the cost-of-capital method described in article 37 of the Delegated Regulation.

The claims provision recognized on the Solvency II balance sheet is a best estimate, which means it does not include any safety margins. The level of uncertainty in the provision estimate is quantified individually for each homogeneous risk group using a stochastic simulation as part of internal modeling.

Reinsurance recoverables are of no material significance to ARAG SE.

The calculation of technical provisions is subject to some uncertainty because the actual level of claims incurred in the future may differ from current forecasts. The degree of uncertainty can be measured on the basis of the extent to which future cash flows can be predicted. Technical provisions are determined using a wide range of assumptions relating to future trends in claims payments and reported claims. Wherever possible, these assumptions are based on historical patterns or estimates drawn up by experts. The main source of uncertainty in connection with the claims provision is the potential for an unexpectedly high level of late reported claims or payments. The level of uncertainty in relation to both the premiums provision and the claims provision is quantified individually for each homogeneous risk group as part of internal modeling. The assumptions made are regularly reviewed, particularly as part of the validation process, and the uncertainty inherent in the technical provisions can therefore be considered manageable from an overall perspective.

No transitional measures have been applied for calculating the technical provisions at ARAG SE. There were no changes in the recognition and valuation methods compared with the previous year.

Differences in the carrying amounts of the technical provisions under the HGB and those calculated for regulatory purposes arise for the following reasons:

**Purpose** The overriding principle that shapes the HGB balance sheet is the protection of creditors. This is particularly applicable to insurance companies: Technical provisions therefore have to be recognized in an amount that, according to prudent business practice, ensures the obligations under insurance policies can always be met.

The purpose of the Solvency II balance sheet is to present the economic capital as of the balance sheet date. Obligations are therefore recognized at their likely present value rather than at a prudently calculated nominal amount.

**Calculation method** The principle of itemized valuation applies to the HGB balance sheet. Therefore, the obligations are inventoried and valued individually using a prudently estimated settlement value. Time and quantity are not explicitly taken into account, but are indirectly factored into the valuation assumptions used to determine the average value of an obligation.

According to the principles of valuation for solvency purposes, the entire portfolio is valued rather than the individual claims. The quantitative data plays only a minor role. The expected payments from the portfolio are estimated as the total of all probable payments until final settlement. This provides an implicit consideration of risk in the valuation of the portfolio. The expected payments are discounted to the valuation date.

**Time aspect of valuations** The valuation rules under the HGB do not take account of the time to maturity in relation to technical provisions. According to supervisory principles, all payments are discounted to the balance sheet date.

### Technical provisions – non-life

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Technical provisions – non-life (excluding health)	0	1,303,085	-1,303,085	0	0
Technical provisions calculated as a whole	0	0	0	0	0
Best estimate	967,801	0	967,801	985,046	-17,244
Risk margin	28,418	0	28,418	32,781	-4,363
<b>Total technical provisions – non-life</b>	<b>996,219</b>	<b>1,303,085</b>	<b>-306,867</b>	<b>1,017,827</b>	<b>-21,608</b>

The overall valuation difference for technical provisions – non-life was €306,867 thousand (the carrying amount calculated for solvency purposes was lower than the HGB amount). This difference is attributable to the qualitative recognition and valuation differences, which are described in detail above for each regime, and to the aforementioned different perspectives. There were no changes in the recognition and valuation methods compared with the previous year.

The total carrying amount of the technical provisions in accordance with Solvency II declined by €21,608 thousand year on year. As of December 31, 2017, the economic value of the claims provisions for each ARAG branch was revalued at segment level and definitively determined at the annual Reserve Committee meeting. At overall level, the provision for outstanding payments relating to claims incurred rose by €8,019 thousand as a consequence of the growth in business. The premiums provision fell by €25,263 thousand as a result of the decline in expenses for future claims, which was mainly attributable in turn to a contraction in the cost ratio. The risk margin changed more or less in line with the change in the solvency capital requirement for future periods, as a result of which there was a decline of €4,363 thousand in this figure.

### Technical provisions – health (similar to non-life)

As of December 31, 2017, ARAG SE had not recognized any technical provisions for health insurance (similar to non-life).

**Technical provisions – life (excluding index-linked and unit-linked)**

As of December 31, 2017, ARAG SE had not recognized any technical provisions for life insurance (excluding index-linked and unit-linked insurance).

**Technical provisions – life (excluding health and index-linked and unit-linked)**

As of December 31, 2017, ARAG SE had not recognized any technical provisions for life insurance (excluding health and index-linked and unit-linked insurance).

**Technical provisions – index-linked and unit-linked**

As of December 31, 2017, ARAG SE had not recognized any technical provisions for index-linked and unit-linked insurance.

**Reinsurance recoverables**

Reinsurance recoverables are the reinsurers' share of the technical provisions. In the case of outward reinsurance business, this means that the figure for reinsurance recoverables equates to the reinsurers' share of the provisions for direct insurance business. Reinsurance cover encompasses liability peaks from individual risks, as needed.

For regulatory purposes, the gross provisions are reported on the liabilities side of the balance sheet without deducting reinsurance recoverables. However, the reinsurers' share is reported as an asset on the other side of the balance sheet. Retrospective and prospective markdowns are recognized to take into account the default risk on the part of reinsurers.

In accordance with the HGB, nominal amounts are recognized, these amounts being determined on the basis of the reinsurance treaties.

On the HGB balance sheet, technical provisions are recognized using a net approach in which the gross amount of the obligation is reduced by the portion covered by outward reinsurance.

The difference between the Solvency II and HGB figures is attributable to this difference in the valuation methods.

On the Solvency II balance sheet, the reinsurance recoverables are reported under assets (see chapter D.1).

**Other technical provisions**

The equalization provision (€16,873 thousand) and the lapse provision (€690 thousand) are reported under miscellaneous technical provisions on the HGB balance sheet. As the Solvency II balance sheet is a strictly statistical exercise, no items to smooth out future fluctuations in the course of business are recognized under other technical provisions (the equivalent line item). For Solvency II purposes, lapse risk is already included in the best estimate item under technical provisions – non-life.

## D.3 Other Liabilities

### Comparison of other liabilities on the HGB balance sheet and Solvency II balance sheet

#### Other liabilities as of December 31, 2017

(€'000)

<b>Contingent liabilities</b>
<b>Provisions other than technical provisions</b>
<b>Pension benefit obligations</b>
<b>Deposits from reinsurers</b>
<b>Deferred tax liabilities</b>
<b>Derivatives</b>
<b>Debts owed to credit institutions</b>
<b>Financial liabilities other than debts owed to credit institutions</b>
Insurance & intermediaries payables
Reinsurance payables
Payables (trade, not insurance)
<b>Subordinated liabilities</b>
Subordinated liabilities not in basic own funds
Subordinated liabilities in basic own funds
<b>Any other liabilities, not elsewhere shown</b>
<b>Total liabilities</b>

	Solvency II as of Dec. 31, 2017	HGB as of Dec. 31, 2017	Difference as of Dec. 31, 2017	Solvency II as of Dec. 31, 2016	Solvency II year-on-year change
	0	0	0	0	0
	90,808	81,332	9,476	84,239	6,569
	221,400	172,271	49,130	220,372	1,029
	1,458	1,458	0	1,510	-51
	177,399	11	177,388	169,235	8,163
	0	0	0	0	0
	0	0	0	0	0
	33,879	33,879	0	35,449	-1,570
	2,136	2,136	0	1,879	257
	48,835	48,835	0	44,023	4,813
	<b>84,850</b>	<b>84,850</b>	<b>0</b>	<b>81,351</b>	<b>3,500</b>
	0	0	0	0	0
	30,000	30,000	0	33,748	-3,748
	<b>30,000</b>	<b>30,000</b>	<b>0</b>	<b>33,748</b>	<b>-3,748</b>
	127	127	0	202	-75
	<b>606,042</b>	<b>370,049</b>	<b>235,993</b>	<b>590,656</b>	<b>15,386</b>

### Contingent liabilities

ARAG SE currently does not have any contingent liabilities that have become a liability that has to be recognized.

### Provisions other than technical provisions

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total provisions other than technical provisions</b>	<b>90,808</b>	<b>81,332</b>	<b>9,476</b>	<b>84,239</b>	<b>6,569</b>

The provisions other than technical provisions are recognized in the amount that is necessary according to prudent business practice. If the liability's settlement period is more than twelve months, they are discounted.

A long-service provision was recognized in the year under review for long-service awards to be paid to employees. A residual maturity of 15 years was assumed. The seven-year average discount rate used by Deutsche Bundesbank was 2.80 percent. 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. In 2017, a provision was recognized in accordance with the pre-retirement part-time employment agreement for the private insurance industry dated June 11, 1997 and the pronouncement of the Institute of Public Auditors in Germany (IDW) dated November 18, 1998. A residual maturity of 15 years was assumed. The seven-year average discount rate used by Deutsche Bundesbank was 2.80 percent. 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 was taken into account. A bank guarantee was provided as collateral for the provisions pursuant to section 8a of the German Pre-retirement Part-time Employment Act (AltTZG).

For solvency purposes, provisions for long-service awards, early retirement obligations, and pre-retirement part-time employment obligations are valued using the projected unit credit method (PUC method) as required by International Accounting Standard (IAS) 19. The discount rate is determined on the basis of the yields achieved for senior industrial bonds on the balance sheet date. Expected growth in income (2.5 percent) and the Company's projections for staff turnover (1.5 percent) are taken into account. The amount calculated in this way equates to the economic value. Other provisions are valued on the basis of the best estimate of the expected settlement amount. The residual maturity for all provisions is less than one year. On grounds of materiality, they were not discounted.

Due to the use of different valuation methods, the obligations recognized under miscellaneous provisions were €9,476 thousand higher on the Solvency II balance sheet than the value on the HGB balance sheet. The year-on-year rise in the Solvency II carrying amount was largely explained by a drop in the level of interest rates on the IAS 19 term structure used to discount the cash flows back to the reporting date. There were no changes in the recognition and valuation methods compared with the previous year.

### Pension benefit obligations

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total pension benefit obligations</b>	<b>221,400</b>	<b>172,271</b>	<b>49,130</b>	<b>220,372</b>	<b>1,029</b>

In accordance with standard international practice, the pension benefit obligations are calculated using the PUC method 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. The following parameters were used to calculate the obligations:

- Pension age: earliest possible age under the German Pension Age Reform Act (RVAGAnpG)
- Annual increase in salaries: 2.5 percent
- Annual increase in pension benefits: 1.75 percent (Spain: 2.5 percent)
- Staff turnover: 1.5 percent, reflecting the generally observable age-dependent average for the industry.

The forecast future payments are discounted to the valuation date. 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.

Existing assets from reinsurance were offset against the defined benefit obligation (€995.3 thousand). In addition, securities with a fair value of €2,691.4 thousand were offset against the present value of the obligation.

The method used to calculate the provision for pensions and other post-employment benefits for solvency purposes is fundamentally the same as the method under the HGB. The only difference is that the discount rate is determined on the basis of the coupon on senior fixed-income industrial bonds. In line with the requirements of IAS 19, this is represented as an interest-rate curve that shows the individual interest rates depending on the actual maturity of the individual obligation.

The different discount rates gave rise to a difference of €49,130 thousand by which the economic value exceeded the HGB value. Under the HGB, the provisions for pensions and other post-employment benefits are recognized using a higher discount rate, so they are discounted to a greater degree. The year-on-year rise in the Solvency II carrying amount was largely explained by a drop in the level of interest rates on the IAS 19 term structure used to discount the cash flows back to the reporting date. There were no changes in the recognition and valuation methods compared with the previous year.

### Deposits from reinsurers

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total deposits from reinsurers</b>	<b>1,458</b>	<b>1,458</b>	<b>0</b>	<b>1,510</b>	<b>-51</b>

Deposits received from reinsurers are recognized at their repayment amount on the HGB balance sheet. They are not discounted.

The economic value of those maturing within twelve months is based on the nominal amount. If the maturity period is longer (more than twelve months), the economic value is determined using the present value method.

There were no valuation differences between the Solvency II balance sheet as of December 31, 2017 and the HGB balance sheet as of December 31, 2017 because the maturity period did not exceed twelve months. The year-on-year decline in the Solvency II carrying amount was mainly caused by a contractual adjustment of the deposits from reinsurers. There were no changes in the recognition and valuation methods compared with the previous year.

### Deferred tax liabilities

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total deferred tax liabilities</b>	<b>177,399</b>	<b>11</b>	<b>177,388</b>	<b>169,235</b>	<b>8,164</b>

If differences arise between the carrying amounts on the Solvency II balance sheet and those in the tax base and these differences are expected to reverse in subsequent years, deferred taxes are recognized on the Solvency II balance sheet in respect of these differences using separate entity-specific tax rates determined according to the country in which the registered office of the permanent establishment/branch 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 will only reverse in the event of any liquidation.

Future tax expense resulting from the reversal effects is always recognized. Deferred taxes from tax group subsidiaries (companies controlled by the parent company and/or with which a profit-and-loss transfer agreement has been concluded) are recognized by the parent company because the income of the tax group is aggregated for tax purposes and taxed overall at the level of the parent company.

The deferred tax liabilities represent an overall expense for the Company. This is because the deferred tax liabilities are dominant on the Solvency II balance sheet and an analysis of the timing of the reversal effects proves that the time until reversal of the deferred tax expense is shorter than the time until reversal of the deferred tax benefit. The expense thus materializes earlier than the benefit.

Unlike on the HGB balance sheet, deferred tax assets and liabilities are not netted on the Solvency II balance sheet and are shown separately. On the Solvency II balance sheet, deferred tax liabilities arise largely as a result of investments being recognized at a higher value and technical provisions at a lower value. The year-on-year rise in the Solvency II carrying amount was mainly caused by a further divergence between tax base and Solvency II carrying amounts. There were no changes in the recognition and valuation methods compared with the previous year.

### Derivatives

No derivatives were recognized by ARAG SE as of December 31, 2017.

### Debts owed to credit institutions

ARAG SE did not have any debts owed to credit institutions as of December 31, 2017.

### Financial liabilities other than debts owed to credit institutions

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Insurance & intermediaries payables	33,879	33,879	0	35,449	-1,570
Reinsurance payables	2,136	2,136	0	1,879	257
Payables (trade, not insurance)	48,835	48,835	0	44,023	4,813
<b>Total financial liabilities other than debts owed to credit institutions</b>	<b>84,850</b>	<b>84,850</b>	<b>0</b>	<b>81,351</b>	<b>3,500</b>

Insurance and intermediaries payables are valued at their nominal amount. All non-interest-bearing liabilities are valued at the higher of their nominal amount or settlement value.

The economic value of those maturing within twelve months is based on the nominal amount. If the maturity period is longer (more than twelve months), the economic value is determined using the present value method. No adjustments are made if ARAG SE's credit rating changes. There are no valuation differences between the Solvency II and HGB carrying amounts. The year-on-year decline in the Solvency II carrying amount was mainly attributable to the normal continuation of business operations. There were no changes in the recognition and valuation methods compared with the previous year.

Reinsurance payables are recognized at their settlement value. There are no differences in their recognition and valuation on the HGB and Solvency II balance sheets. The year-on-year increase in the Solvency II carrying amount was largely caused by billing close to the reporting date. There were no changes in the recognition and valuation methods compared with the previous year.

Payables (trade, not insurance) are recognized at their settlement value. All non-interest-bearing liabilities are valued at the higher of their nominal amount or settlement value. There are no differences in their recognition and valuation on the HGB and Solvency II balance sheets. The year-on-year rise in the Solvency II carrying amount was mainly attributable to the higher business volume, the resulting increase in insurance tax, and more extensive services from Group companies billed as of the reporting date. There were no changes in the recognition and valuation methods compared with the previous year.

### Subordinated liabilities

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
Subordinated liabilities not in basic own funds	0	0	0	0	0
Subordinated liabilities in basic own funds	32,601	30,000	2,601	33,748	-1,147
<b>Total subordinated liabilities</b>	<b>32,601</b>	<b>30,000</b>	<b>2,601</b>	<b>33,748</b>	<b>-1,147</b>

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 nominal value of €30,000 thousand has a fixed maturity of ten years and will be redeemed on July 29, 2024. The subordinated bearer bonds are recognized at their settlement amount. These bonds are not negotiable in Germany on a regulated market within the meaning of section 2 (5) of the German Securities Trading Act (WpHG).

On the Solvency II balance sheet, the subordinated liabilities are discounted with the risk-free interest rate derived from investment-grade industrial bonds, modified by the value of ARAG's different credit rating at the time the subordinated bond was issued on July 29, 2014. This results in an interest rate that is lower than the bond's nominal interest rate (4.826 percent). Because of the discounting, the value on the Solvency II balance sheet as of December 31, 2017 was €2,601 thousand higher than the value on the HGB balance sheet. The Solvency II carrying amount declined year on year because of the shorter time to maturity.

There were no changes in the recognition and valuation methods compared with the previous year.

#### Any other liabilities, not elsewhere shown

(€'000)	SII as of Dec. 31, 2017	HGB as of Dec. 31, 2017	SII/HGB difference as of Dec. 31, 2017	SII as of Dec. 31, 2016	SII year-on- year change
<b>Total of any other liabilities, not elsewhere shown</b>	127	127	0	202	-75

Any other liabilities, not elsewhere shown are recognized at their settlement value. All non-interest-bearing liabilities are valued at the higher of their nominal amount or settlement value.

The economic value of those maturing within twelve months is based on the nominal amount. If the maturity period is longer (more than twelve months), the economic value is determined using the present value method. No adjustments are made if ARAG SE's credit rating changes. No such liabilities with a maturity of more than twelve months were discounted.

There are no valuation differences between the Solvency II and HGB carrying amounts. The year-on-year decline in the Solvency II carrying amount was mainly attributable to the normal continuation of business operations because the amount concerned consisted of deferred income in accordance with the HGB.

There were no changes in the recognition and valuation methods compared with the previous year.

## D.4 Alternative Methods for Valuation

No alternative valuation methods other than those listed in sections D.1 to D.3 inclusive have been used.

## D.5 Any Other Information

Chapters D.1 to D.4 inclusive contain all of the important information about the valuation for solvency purposes.

## E. Capital Management

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## E.1 Own Funds

### Objectives, guidance, and procedures for managing own funds

In 2017, Solvency II balance sheets were prepared for the planning horizon on the basis of the budgeted results of operations. The existing internal capital management guidance states that if it is identified that solvency coverage is about to fall below a threshold value that is higher than the intervention value specified by the German Federal Financial Supervisory Authority (BaFin), various measures should be considered to offset the fall in the level of coverage. If such a situation were to be identified, the governing bodies would be informed in accordance with the escalation path specified in the Company's capital management policy. Various measures would then be drawn up and examined as to their suitability before being submitted in turn to the decision-making bodies for implementation. The examination of whether one or more of the measures would be suitable would involve assessing when the measures could be implemented, what effect they would have, and whether multiple measures could be implemented in parallel.

In view of the existing solvency profile, the coverage ratio is not currently expected to fall below the internal reporting threshold, and certainly not below regulatory requirements. If, contrary to expectations, too great a fall in solvency coverage were to materialize in the medium term, the following measures would be considered with a view to increasing own funds:

- Restriction on distribution
- Additional payment into the capital reserve, increase in share capital
- Borrowing pursuant to section 89 (3) no. 2 VAG.

Subject to prior authorization from the supervisory authority, subordinated liabilities can also be used as basic own funds by companies that do not have securities admitted to trading on a regulated market in the EU. This method does provide a way of significantly bolstering own funds, although operating performance is adversely impacted by the interest that needs to be paid.

In 2017, the Company did not identify any need to strengthen components of basic own funds within its planning horizon. Accordingly, none of the measures listed above were drawn up or submitted to the decision-making bodies for implementation.

### Components and quality of own funds

As of December 31, 2017, ARAG SE held basic own funds in the form of an excess of assets over liabilities of €1,162,266 thousand according to the Solvency II balance sheet. It also had a subordinated liability of €32,601 thousand classified as own funds. This registered bond has a fixed maturity of ten years and will be redeemed on July 29, 2024. In the event of liquidation, it will be subordinate to all other liabilities. According to the proposal for appropriation of the profit recognized on the HGB balance sheet, a sum of €20,000 thousand will be distributed to shareholders as dividends.

This results in eligible own funds of €1,174,867 thousand, split between the different capital classes as follows: Tier 1 own funds of €1,142,266 thousand and Tier 2 own funds of €32,601 thousand.

The equity on the HGB balance sheet can be reconciled to eligible own funds as follows:

### Reconciliation of the equity on the HGB balance sheet to eligible own funds

(€'000)	Dec. 31, 2017	Dec. 31, 2016
<b>Equity as of December 31 on the HGB balance sheet</b>	<b>439,405</b>	<b>422,374</b>
Elimination of intangible assets	- 7,658	- 8,329
Additional deferred tax assets	72,806	69,732
Revaluation of land and buildings held for own use (fair value)	8,732	11,983
Revaluation of investments	566,432	777,749
Revaluation of other loans and mortgages	0	284
Revaluation of reinsurers' share of technical provisions	- 3,287	- 2,932
No separate recognition of miscellaneous technical provisions, gross	306,867	245,277
No separate recognition of miscellaneous technical provisions	17,563	14,676
Revaluation of miscellaneous provisions	- 9,476	- 6,093
Revaluation of provisions for pensions and other post-employment benefits	- 49,130	- 56,057
Additional deferred tax liabilities recognized	- 177,388	- 169,235
Revaluation of the subordinated liabilities included in basic own funds	- 2,601	- 3,748
<b>Excess of assets over liabilities according to the Solvency II balance sheet</b>	<b>1,162,266</b>	<b>1,295,680</b>
Additional basic own funds resulting from subordinated liabilities	32,601	33,748
<b>Total basic own funds as of December 31</b>	<b>1,194,867</b>	<b>1,329,428</b>
Foreseeable dividend	- 20,000	- 15,000
<b>Total eligible own funds as of December 31</b>	<b>1,174,867</b>	<b>1,314,428</b>

Please refer to chapter D. for information on the qualitative differences between the equity reported in the Company's financial statements and the excess of assets over liabilities calculated for solvency purposes as well as on the year-on-year changes.

**Own funds reconciliation reserve**

(€'000)	Total	Tier 1 own funds	Tier 2 own funds	Tier 3 own funds
Share capital	100,000	100,000	0	0
Share premium account related to ordinary share capital	0	0	0	0
Reconciliation reserve	1,042,266	1,042,266	0	0
<b>Basic own funds</b>	<b>1,142,266</b>	<b>1,142,266</b>	<b>0</b>	<b>0</b>
Ancillary own funds (subordinated liabilities)	32,601		32,601	0
<b>Eligible own funds</b>	<b>1,174,867</b>	<b>1,142,266</b>	<b>32,601</b>	<b>0</b>

As of December 31, 2017, the reconciliation reserve amounted to €1,042,266 thousand and consisted of revenue reserves of €225,600 thousand, valuation differences of €722,861 thousand, capital reserves pursuant to section 272 (2) no. 4 HGB of €81,773 thousand, and the net retained profit (reduced by the planned dividend) of €12,032 thousand.

All quantitative disclosures relate to the figures in the quantitative reporting formats set out in the Appendix.

## E.2 Solvency Capital Requirement and Minimum Capital Requirement

ARAG SE uses a partial internal model to calculate the solvency capital requirement. In this certified model, the modules for market risk, non-life underwriting risk, and counterparty default risk are calculated using internal modeling. The other risk modules (e.g. operational risk) and the aggregation of the risk modules for the overall solvency requirement are based on the standardized approach.

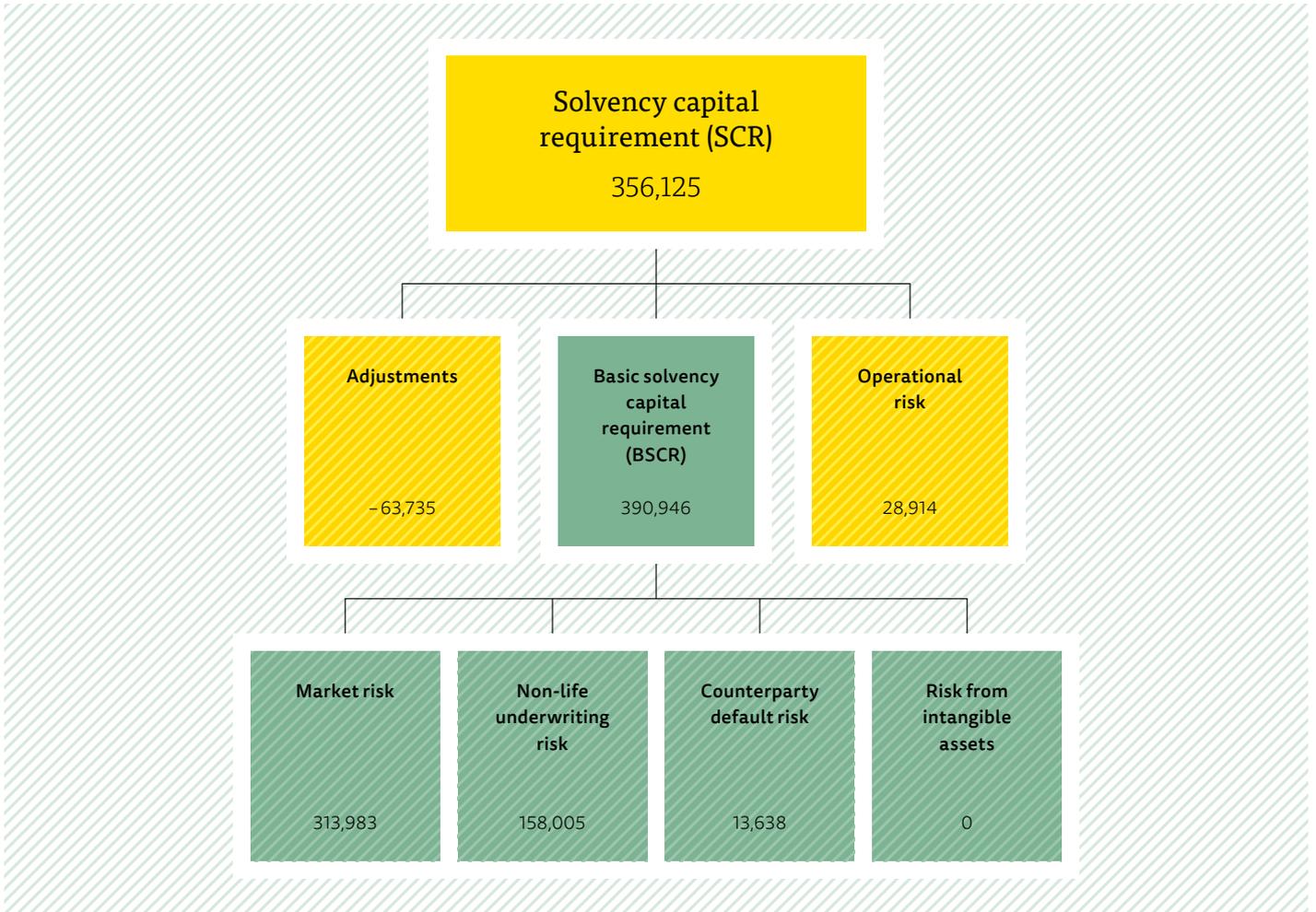
The solvency capital requirement declined by 14 percent year on year, from €416,034 thousand as of December 31, 2016 to €356,125 thousand as of the reporting date. The main driver behind this change was the sharp fall in market risk, caused by the decline in equity investment risk following the disposal of ARAG Lebensversicherungs-AG. Please refer to chapter C. 'Risk Profile' for further information on the changes in the individual risks. At 329.9 percent as of December 31, 2017, the coverage ratio was significantly higher than the regulatory requirement and, in ARAG SE's view, constitutes a substantial risk buffer for customers. This represented a further rise of 14 percentage points compared with the figure of 316 percent as of December 31, 2016, with the fall in the solvency capital requirement being substantially greater than that in own funds.

Neither a simplified calculation of the SCR standard formula nor undertaking-specific parameters (USPs) are used in any of the modules.

The minimum capital requirement is calculated on the basis of the technical provisions (excluding the risk margin) and net premiums written in the past twelve months in each line of business; it must not fall below 25 percent and not exceed 45 percent of the solvency capital requirement. As of December 31, 2017, the minimum capital requirement was €160,256 thousand (December 31, 2016: €170,060 thousand), which equated to 45 percent of the solvency capital requirement at that time and resulted in a coverage ratio for the minimum capital requirement of 733 percent (December 31, 2016: 773 percent).

The final amount of the solvency capital requirement is still subject to verification by the supervisory authority. All quantitative disclosures relate to the figures in the quantitative reporting formats set out in the Appendix.

## EIOPA risk tree for ARAG SE (€'000)



**Solvency capital requirement (SCR)** is the amount of own funds required to be held in case of an unlikely but large loss.

**Adjustments** contain the loss-absorbing capacity of technical provisions and deferred taxes.

**Basic solvency capital requirement (BSCR)** is the sum of the correlated individual risks or the solvency capital requirement (SCR) before adjustments, operational risk (OpRisk), and any non-controlled participations (NCPs).

**Operational risk** quantifies the risk arising from inadequate or failed internal processes, personnel, or systems, or from external events.

**Market risk** is the risk arising from the level or volatility of market prices of financial instruments that have an impact on the value of the assets and liabilities of a company.

**Non-life underwriting risk** is the risk arising from the risks covered and the processes used in the course of property insurance business.

**Counterparty default risk** reflects possible losses due to unexpected default or deterioration in the credit standing of counterparties and debtors in the insurance business and of reinsurance companies over the following twelve months.

**Risks from intangible assets** result from the underlying risks in the form of price fluctuations or illiquidity and from those that are derived directly from the specificity of the assets.

## E.3 Use of the Duration-Based Equity Risk Sub-Module in the Calculation of the Solvency Capital Requirement

Using the duration-based equity risk sub-module in the calculation of the solvency capital requirement is not relevant to ARAG SE.

## E.4 Differences Between the Standard Formula and Any Internal Model Used

ARAG SE's partial internal model was approved on December 10, 2015 when BaFin certified the model. At the start of the initial consultation phase, ARAG SE had examined the possibilities offered by the standardized approach and quickly realized that the only way to adequately represent the risks was by using a partial internal model. The six months required for the approval process were preceded by a five-year pre-application phase, during which in-depth discussions were held with BaFin, an appropriate governance structure was established (including the Risk Committee and Internal Model Committee described earlier), and a wide range of elements were introduced – with a view to using the partial internal model – such as a limit system, internal risk modeling, risk-oriented management, stakeholder-oriented reporting, and uniform quality standards for data.

From the perspective of ARAG SE, it was important to ensure that the development of the model reflected, as far as possible, the conservative investment and underwriting policy dictated by the ownership structure. ARAG SE's focus was therefore to fulfill a number of prerequisites that highlighted the greater benefit of a partial internal model compared with the standardized approach:

- **Experience:** ARAG SE has operated successfully in German and international insurance markets for 80 years. In its relationships with customers, the Company sees itself as rather more than just an organization for reimbursing costs. It is always looking for new ways to provide comprehensive assistance for the customer if the worst-case scenario should arise. At ARAG SE, customer benefit and customer protection go hand in hand at all times.
- **Business model:** ARAG SE is part of the ARAG Group, the largest family enterprise in the German insurance industry, and is one of the world's three leading providers of legal insurance. The Company positions itself as a legal insurance provider focusing on private customers and small and medium-sized enterprises (SMEs). It is not involved in diversified corporate business with the special risks typical of this business.

- **Independence:** Independence is at the core of the ARAG Group, the largest family enterprise in the German insurance industry, and plays a key role at ARAG SE. It provides a great deal of business latitude, enabling the Company to make decisions without having to worry about short-term shareholder returns. ARAG SE also pursues a conservative business strategy with a long-term focus, offering stability, reliability, and continuity to both the Company and its customers.
- **International presence:** In addition to the Group headquarters in Düsseldorf, ARAG SE currently maintains branches in Austria, Belgium, Greece, Italy, the Netherlands, Portugal, Slovenia, and Spain. The Group is a leader in many international legal insurance markets. Legal insurance products precisely tailored to the needs of customers in each market provide the recipe for success. The highly effective processes for transferring knowledge within the Group also mean that successful product ideas can be quickly adapted for use in other countries.
- **Quality:** The success of the ARAG Group is based on quality and the particular innovative strength of the Group. The Group is always open to new ideas – reflected, not least, in its state-of-the-art insurance products and services. These are consistently focused on customer needs to ensure that customers enjoy both optimum insurance cover in line with their requirements and also genuine added value and benefits. The high quality of the services is reflected, among other things, in the numerous regular awards and seals of approval received from independent organizations.

This self-image, which is mirrored in the Group's business model, was one of the major factors behind the development of a partial internal model for ARAG SE. ARAG SE's specific risk profile cannot be accurately reflected using the standard formula.

The Company is able to draw on its extensive inhouse knowledge from its many years of experience and its claims history and combine this with a clear product and underwriting policy in order to model the individual risks internally in accordance with its own requirements, thus ensuring the risks can be presented and managed adequately. Furthermore, the extensive reinsurance program is analyzed and modeled separately in the partial internal model of ARAG SE, as is appropriate to a far more reality-based approach to risk modeling.

The internal modeling of market risk enables the scope and structure of the investment portfolio to be examined and analyzed more accurately. Furthermore, the use of an economic scenario generator enables capital market risks to be depicted much more precisely than with the scenario-based key figures used in the standardized approach. This is particularly the case for the non-linear maturity profiles that can be found with callable bonds, for example, or for the risk-based valuation of government bonds. In both cases – i.e. in the case of both internally modeled market risk and internally modeled non-life underwriting risk – the results are used for management on the basis of key risk indicators adjusted to the Company's specific requirements.

ARAG SE's partial internal model draws on the following internally modeled modules: market risk, non-life underwriting risk, and counterparty default risk. The non-life underwriting risk module and the market risk module are modeled up to the top module level as a distribution. The counterparty default risk module is scenario-based at the top level and contains parts of the standard formula. The counterparty default risk arising in connection with securities is integrated into the market risk module.

### **Probability distribution forecast**

The interest-rate, spread, equity, real-estate, and currency sub-risks are analyzed as part of the internal modeling of market risk. The concentration sub-risk is classified as not material and therefore not analyzed. However, changes in this sub-risk are continuously monitored as part of the validation process. The analysis is carried out according to various criteria, such as asset class, currency area, maturity, and credit quality level. The underlying stochastic models correspond to generally accepted methodologies in financial mathematics. A critical factor in the calculation of risk is the calibration of the underlying risk factors and their correlations. The calibration is carried out for each calculation reference date using the latest market data. Separate performance indices are calibrated on the basis of current risk calculations for relevant strategic equity investments in insurance companies within the ARAG Group.

Non-life underwriting risk comprises the following components: premium risk, reserve risk, and accumulation risk. ARAG SE believes that accumulations of legal insurance represent the catastrophe risk for a legal insurance company. The catastrophe module has therefore been extended to include accumulation risk. The modules do not differ materially from the structure of the standard formula.

In the market risk and non-life underwriting risk modules, stochastic simulations are used to project the Company's own funds one year ahead without taking any tax effects into account. For the market risk and non-life underwriting risk modules, the solvency capital requirement then equates to the value-at-risk around the 99.5 percent quantile of the relevant loss distribution. A going-concern approach is assumed when determining underwriting risk. This means, in particular, that the forecast new business for the coming twelve months is included.

ARAG SE's underwriting portfolio is broken down into various segments according to management and risk considerations. This segmentation enables management-relevant information to be determined from the partial internal model and used for the management of the Company on a value-driven basis. The principle whereby groups sharing similar risk characteristics are modeled is also applied in this segmentation.

In ARAG SE's internal modeling, counterparty default risk is covered partially in the market risk module and partially in the counterparty default risk module. However, between the two modules, all default risk is covered. Those default risks that are not addressed in the market risk module are quantified in the counterparty default risk module. The remaining risks determined in this way are calculated using a factor approach based on the standard formula.

The individual market risk, non-life underwriting risk, and counterparty default risk modules are aggregated into the basic solvency capital requirement using a correlation approach. The total solvency capital requirement is determined by adding the solvency capital requirement for operational risk calculated in accordance with the standard formula and by applying the risk-mitigating effect from deferred taxes. No capital add-ons are recognized.

### Main differences between the internal model and the standard formula for each risk module

The differences between the internal model and the standard formula are explained below for each market risk sub-module.

#### Comparison between the market risk sub-modules in the internal model and the standard formula

Sub-module	Standard formula	Internal model
Interest rate	For each currency area, the risk-free interest-rate term structure is shifted upwards and downwards with maturity-dependent shocks.	A distribution for the underlying interest rate calibrated using current market data is simulated for each currency area and each maturity. Turns and bulges in the risk-free interest-rate term structure are observed in addition to shifts.
Spread	The market values of investments sensitive to spread risk are reduced with a factor dependent on asset class, credit quality level, and maturity.	In the internal model, firstly, a distribution for the underlying spread calibrated using current market data is simulated for each investment class, credit quality level, and maturity. Secondly, a change in the risk classification and payment defaults are simulated for each issuer. In addition to bonds, other items taken into account in this case (in contrast to the standardized approach) include cash exposures and government bonds.
Equities	A factor is used to stress the market values of all equity investments. A distinction is made between equity type 1 (listed equities from an OECD or EEA country), equity type 2 (equities from other countries), strategic equity investments, and qualifying infrastructure. The solvency capital requirements resulting from the 'equity type 1' and 'equity type 2' scenarios are aggregated as the equity solvency capital requirement using a correlation approach.	A distribution of equity performance calibrated using current market data is simulated for each currency area. A similar distribution for private equity investments is also simulated. Separate distributions of performance are calibrated and simulated for strategic equity investments.
Real estate	The market values of all real estate investments are reduced by a particular factor.	A distribution of real estate performance calibrated using current market data is simulated for each currency area.
Currency	The market values of all assets and liabilities denominated in foreign currency are increased/decreased by a particular factor. This gives rise to a currency increase and a currency decrease risk for each currency area, reported as the corresponding loss of own funds.	A distribution for the change in the foreign currency/euro exchange rate calibrated using current market data is simulated for each currency area.
Concentration	An additional risk capital requirement is calculated using a factor approach for exposures that exceed a specified percentage of the total portfolio.	Risk concentrations in bonds and cash exposures are taken into account in the spread module via the default distributions simulated for each issuer. There is no separate calculation of concentration risk in the internal model.

The differences between the internal model and the standard formula in respect of the counterparty default risk module are explained below.

### Comparison between the counterparty default risk module in the internal model and the standard formula

Risk module	Standard formula	Internal model
Default	Cash exposures and various receivables exposures are subjected to a shock using a factor approach.	Only receivables exposures are included because defaults relating to cash exposures are simulated in the market risk module on a stochastic basis. The default risk on receivables is valued in accordance with the standardized approach.

The differences between the internal model and the standard formula are explained below for each non-life underwriting risk sub-module.

### Comparison between the underwriting risk sub-modules in the internal model and the standard formula

Sub-module	Standard formula	Internal model
Premium and reserve risk	A factor-based approach is used in the standard formula. The standard volatility factors (market average) for each line of business are applied to the relevant volume measure (reserve or premiums). Specified correlation parameters are used in a linear correlation approach. Regional diversification is taken into account.	In the partial internal model, casualty and property insurance is broken down into groups of risks sharing similar characteristics and these risk groups form the ARAG segments. The risk calculation is based on company-specific data and internal calibration. Reinsurance is precisely reflected in the model, especially in relation to major losses. The aggregation method follows a copula approach. Well-established actuarial methods are used.
Lapse risk	A stress scenario is applied to the forecast profits from the current portfolio.	A lapse distribution is modeled, with calibration based on company-specific data.
Legal insurance accumulation risk	This risk is not taken into account in the standard formula.	Accumulation events represent a heightened risk in the legal insurance business. ARAG therefore models these losses with its own data using a distribution of the number of claims and claims amounts.

Diversification effects are highlighted by aggregating the risk distributions for the individual sub-risks into the total risk capital requirement. The diversification effect between the modules for ARAG SE amounted to €94,681 thousand. Diversification effects arise if the risks to be aggregated are independent or only partially dependent on each other. Key diversification factors include, for example:

- Classes of insurance or segments – legal insurance disputes involving private or small business customers
- Risk categories – legal insurance disputes from different areas of activity, such as road traffic or employment
- Regions – accumulation of losses in different countries.

To value the diversification effects within ARAG SE's partial internal model, the dependencies between the risk sub-modules and risk categories are quantified. ARAG uses its own historical data to measure the dependencies. The parameters are reviewed annually by a committee of experts to check that they remain plausible.

**Appropriateness of data**

ARAG SE's partial internal model uses a variety of data sources as inputs for calibration and parameterization purposes. The basis is provided by the Company's own data. By using internal historical data for the calibration, it is possible to ensure that the risk profile is modeled accurately and an adequate forecast is generated.

The quality of the data used in the partial internal model's calculations is regularly reviewed. To this end, data quality standards have been laid down in a data quality policy. The objective of the standards is to safeguard the quality and appropriateness of the necessary data over the long term. ARAG examines data quality from the following perspectives:

- Accuracy – data must be error-free, consistent, and trustworthy.
- Completeness – data must be up to date and provide the necessary level of detail and granularity.
- Appropriateness – data must reflect current reality, be relevant to the business, and be fit for the intended purpose.

## **E.5 Non-Compliance with the Minimum Capital Requirement and Non-Compliance with the Solvency Capital Requirement**

Taking a prudent view, ARAG SE does not believe it is exposed to any foreseeable risk of non-compliance with the minimum capital requirement or the solvency capital requirement.

## **E.6 Any Other Information**

The preceding chapters contain all of the important information about capital management.

# Appendix

## S.02.01.02

### Balance sheet

		Solvency II value
		C0010
<b>Assets</b>		
Intangible assets	R0030	0
Deferred tax assets	R0040	72,806
Pension benefit surplus	R0050	0
Property, plant & equipment held for own use	R0060	54,049
Investments (other than assets held for index-linked and unit-linked contracts)	R0070	2,396,055
Property (other than for own use)	R0080	32,856
Holdings in related undertakings, including participations	R0090	817,923
Equities	R0100	1,024
Equities – listed	R0110	244
Equities – unlisted	R0120	781
Bonds	R0130	839,929
Government bonds	R0140	208,570
Corporate bonds	R0150	622,966
Structured notes	R0160	7,310
Collateralized securities	R0170	1,084
Collective investment undertakings	R0180	638,901
Derivatives	R0190	0
Deposits other than cash equivalents	R0200	57,969
Other investments	R0210	7,453
Assets held for index-linked and unit-linked contracts	R0220	0
Loans and mortgages	R0230	9,259
Loans on policies	R0240	0
Loans and mortgages to individuals	R0250	79
Other loans and mortgages	R0260	9,180
Reinsurance recoverables from:	R0270	699
Non-life and health similar to non-life	R0280	699
Non-life excluding health	R0290	699
Health similar to non-life	R0300	0
Life and health similar to life, excluding health and index-linked and unit-linked	R0310	0
Health similar to life	R0320	0
Life excluding health and index-linked and unit-linked	R0330	0
Life index-linked and unit-linked	R0340	0
Deposits to cedants	R0350	49,677
Insurance and intermediaries receivables	R0360	45,442
Reinsurance receivables	R0370	46,740
Receivables (trade, not insurance)	R0380	31,357
Own shares (held directly)	R0390	0
Amounts due in respect of own fund items or initial fund called up but not yet paid in	R0400	0
Cash and cash equivalents	R0410	58,303
Any other assets, not elsewhere shown	R0420	2,739
<b>Total assets</b>	R0500	<b>2,767,127</b>

## S.02.01.02

## Balance sheet

		Solvency II value
<b>Liabilities</b>		<b>C0010</b>
Technical provisions – non-life	R0510	996,219
Technical provisions – non-life (excluding health)	R0520	996,219
Technical provisions calculated as a whole	R0530	0
Best estimate	R0540	967,801
Risk margin	R0550	28,418
Technical provisions – health (similar to non-life)	R0560	0
Technical provisions calculated as a whole	R0570	0
Best estimate	R0580	0
Risk margin	R0590	0
Technical provisions – life (excluding index-linked and unit-linked)	R0600	0
Technical provisions – health (similar to life)	R0610	0
Technical provisions calculated as a whole	R0620	0
Best estimate	R0630	0
Risk margin	R0640	0
Technical provisions – life (excluding health and index-linked and unit-linked)	R0650	0
Technical provisions calculated as a whole	R0660	0
Best estimate	R0670	0
Risk margin	R0680	0
Technical provisions – index-linked and unit-linked	R0690	0
Technical provisions calculated as a whole	R0700	0
Best estimate	R0710	0
Risk margin	R0720	0
Contingent liabilities	R0740	0
Provisions other than technical provisions	R0750	90,808
Pension benefit obligations	R0760	221,400
Deposits from reinsurers	R0770	1,458
Deferred tax liabilities	R0780	177,399
Derivatives	R0790	0
Debts owed to credit institutions	R0800	0
Financial liabilities other than debts owed to credit institutions	R0810	0
Insurance & intermediaries payables	R0820	33,879
Reinsurance payables	R0830	2,136
Payables (trade, not insurance)	R0840	48,835
Subordinated liabilities	R0850	32,601
Subordinated liabilities not in basic own funds	R0860	0
Subordinated liabilities in basic own funds	R0870	32,601
Any other liabilities, not elsewhere shown	R0880	127
<b>Total liabilities</b>	R0900	<b>1,604,862</b>
<b>Excess of assets over liabilities</b>	R1000	<b>1,162,266</b>

## S.05.01.02

## Premiums, claims and expenses by line of business

		Medical expense insurance	Income protection insurance
		C0010	C0020
<b>Premiums written</b>			
Gross – direct business	R0110	0	0
Gross – proportional reinsurance accepted	R0120	0	0
Gross – non-proportional reinsurance accepted	R0130	-	-
Reinsurers' share	R0140	0	0
Net	R0200	0	0
<b>Premiums earned</b>			
Gross – direct business	R0210	0	0
Gross – proportional reinsurance accepted	R0220	0	0
Gross – non-proportional reinsurance accepted	R0230	-	-
Reinsurers' share	R0240	0	0
Net	R0300	0	0
<b>Claims incurred</b>			
Gross – direct business	R0310	0	0
Gross – proportional reinsurance accepted	R0320	0	0
Gross – non-proportional reinsurance accepted	R0330	-	-
Reinsurers' share	R0340	0	0
Net	R0400	0	0
<b>Changes in other technical provisions</b>			
Gross – direct business	R0410	0	0
Gross – proportional reinsurance accepted	R0420	0	0
Gross – non-proportional reinsurance accepted	R0430	-	-
Reinsurers' share	R0440	0	0
Net	R0500	0	0
<b>Expenses incurred</b>	R0550	<b>0</b>	<b>0</b>
<b>Other expenses</b>	R1200	-	-
<b>Total expenses</b>	R1300	-	-



## S.05.01.02

## Premiums, claims and expenses by line of business

		Line of business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)		
		Legal expenses insurance	Assistance	Miscellaneous financial loss
		C0100	C0110	C0120
<b>Premiums written</b>				
Gross – direct business	R0110	614,879	48,637	9,736
Gross – proportional reinsurance accepted	R0120	181,559	14,665	529
Gross – non-proportional reinsurance accepted	R0130	-	-	-
Reinsurers' share	R0140	302	899	0
Net	R0200	796,135	62,403	10,265
<b>Premiums earned</b>				
Gross – direct business	R0210	615,157	47,979	9,804
Gross – proportional reinsurance accepted	R0220	181,373	14,373	557
Gross – non-proportional reinsurance accepted	R0230	-	-	-
Reinsurers' share	R0240	302	899	0
Net	R0300	796,227	61,453	10,362
<b>Claims incurred</b>				
Gross – direct business	R0310	251,348	22,763	25
Gross – proportional reinsurance accepted	R0320	60,421	13,791	-191
Gross – non-proportional reinsurance accepted	R0330	-	-	-
Reinsurers' share	R0340	2,224	264	0
Net	R0400	309,545	36,290	-166
<b>Changes in other technical provisions</b>				
Gross – direct business	R0410	192	0	0
Gross – proportional reinsurance accepted	R0420	0	0	0
Gross – non-proportional reinsurance accepted	R0430	-	-	-
Reinsurers' share	R0440	0	0	0
Net	R0500	192	0	0
<b>Expenses incurred</b>	R0550	<b>477,589</b>	<b>29,212</b>	<b>6,225</b>
<b>Other expenses</b>	R1200	-	-	-
<b>Total expenses</b>	R1300	-	-	-

Line of business for: accepted non-proportional reinsurance					Total
Health	Casualty	Marine, aviation, transport	Property		
C0130	C0140	C0150	C0160		C0200
0	0	0	0		673,252
0	0	0	0		196,752
-	-	-	-		0
0	0	0	0		1,201
0	0	0	0		868,803
0	0	0	0		672,940
0	0	0	0		196,303
-	-	-	-		0
0	0	0	0		1,201
0	0	0	0		868,041
0	0	0	0		274,136
0	0	0	0		74,021
-	-	-	-		0
0	0	0	0		2,488
0	0	0	0		345,669
0	0	0	0		192
0	0	0	0		0
-	-	-	-		0
0	0	0	0		0
0	0	0	0		192
<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>		<b>513,026</b>
-	-	-	-		-
-	-	-	-		<b>513,026</b>

## S.05.01.02

## Premiums, claims and expenses by line of business

		Health insurance	Insurance with profit participation
		C0210	C0220
<b>Premiums written</b>			
Gross	R1410	0	0
Reinsurers' share	R1420	0	0
Net	R1500	0	0
<b>Premiums earned</b>			
Gross	R1510	0	0
Reinsurers' share	R1520	0	0
Net	R1600	0	0
<b>Claims incurred</b>			
Gross	R1610	0	0
Reinsurers' share	R1620	0	0
Net	R1700	0	0
<b>Changes in other technical provisions</b>			
Gross	R1710	0	0
Reinsurers' share	R1720	0	0
Net	R1800	0	0
<b>Expenses incurred</b>	R1900	0	0
<b>Other expenses</b>	R2500	-	-
<b>Total expenses</b>	R2600	-	-



## S.05.02.01

## Premiums, claims and expenses by country

		Home country
		<b>C0010</b>
	R0010	-
		<b>C0080</b>
<b>Premiums written</b>		
Gross – direct business	R0110	349,202
Gross – proportional reinsurance accepted	R0120	21,922
Gross – non-proportional reinsurance accepted	R0130	-
Reinsurers' share	R0140	300
Net	R0200	370,825
<b>Premiums earned</b>		
Gross – direct business	R0210	345,575
Gross – proportional reinsurance accepted	R0220	21,922
Gross – non-proportional reinsurance accepted	R0230	-
Reinsurers' share	R0240	0
Net	R0300	367,198
<b>Claims incurred</b>		
Gross – direct business	R0310	187,729
Gross – proportional reinsurance accepted	R0320	20,038
Gross – non-proportional reinsurance accepted	R0330	-
Reinsurers' share	R0340	1,017
Net	R0400	206,750
<b>Changes in other technical provisions</b>		
Gross – direct business	R0410	221
Gross – proportional reinsurance accepted	R0420	0
Gross – non-proportional reinsurance accepted	R0430	0
Reinsurers' share	R0440	0
Net	R0500	221
<b>Expenses incurred</b>	R0550	<b>187,257</b>
<b>Other expenses</b>	R1200	-
<b>Total expenses</b>	R1300	-

Top 5 countries (by amount of gross premiums written) - non-life obligations						Total top 5 and home country
C0020	C0030	C0040	C0050	C0060	C0070	
BE	ES	IT	NL	AT		-
C0090	C0100	C0110	C0120	C0130		C0140
23,774	105,104	33,505	92,531	61,072		665,189
743	33,936	90,014	49,929	0		196,544
-	-	-	-	-		0
-0	901	0	0	0		1,201
24,517	138,138	123,519	142,460	61,072		860,531
23,548	104,112	32,522	98,458	60,666		664,881
743	34,561	88,983	49,885	0		196,095
-	-	-	-	-		0
-0	901	0	0	0		1,201
24,291	137,771	121,505	148,343	60,666		859,774
10,427	33,310	9,672	15,740	15,630		272,508
422	25,353	20,960	7,298	-30		74,041
-	-	-	-	-		0
16	1,465	0	0	-10		2,488
10,833	57,198	30,632	23,038	15,610		344,061
0	0	0	0	-29		192
0	0	0	0	0		0
0	0	0	0	0		0
0	0	0	0	0		0
0	0	0	0	-29		192
<b>12,139</b>	<b>73,694</b>	<b>87,050</b>	<b>111,745</b>	<b>28,331</b>		<b>500,216</b>
-	-	-	-	-		-
-	-	-	-	-		<b>500,216</b>

## S.05.02.01

## Premiums, claims and expenses by country

		Home country	
			<b>C0150</b>
	R1400		-
			<b>C0220</b>
<b>Premiums written</b>			
Gross	R1410		
Reinsurers' share	R1420		
Net	R1500		
<b>Premiums earned</b>			
Gross	R1510		
Reinsurers' share	R1520		
Net	R1600		
<b>Claims incurred</b>			
Gross	R1610		
Reinsurers' share	R1620		
Net	R1700		
<b>Changes in other technical provisions</b>			
Gross	R1710		
Reinsurers' share	R1720		
Net	R1800		
<b>Expenses incurred</b>	R1900		
<b>Other expenses</b>	R2500		-
<b>Total expenses</b>	R2600		-



## S.17.01.02

## Non-life technical provisions

		Medical expense insurance	Income protection insurance
		C0020	C0030
<b>Technical provisions calculated as a whole</b>	R0010	-	-
Total recoverables from reinsurance/SPV and finite re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole	R0050	-	-
<b>Technical provisions calculated as a sum of BE and RM</b>			
Best estimate			
Premium provisions			
Gross	R0060	-	-
Total recoverable from reinsurance/SPV and finite re after the adjustment for expected losses due to counterparty default	R0140	-	-
Net best estimate of premium provisions	R0150	-	-
<b>Claims provisions</b>			
Gross	R0160	-	-
Total recoverable from reinsurance/SPV and finite re after the adjustment for expected losses due to counterparty default	R0240	-	-
<b>Net best estimate of claims provisions</b>	R0250	-	-
<b>Total best estimate - gross</b>	R0260	-	-
<b>Total best estimate - net</b>	R0270	-	-
<b>Risk margin</b>	R0280	-	-
<b>Amount of the transitional on technical provisions</b>			
Technical provisions calculated as a whole	R0290	-	-
Best estimate	R0300	-	-
Risk margin	R0310	-	-
<b>Technical provisions - total</b>			
Technical provisions - total	R0320	-	-
Recoverable from reinsurance contract/SPV and finite re after the adjustment for expected losses due to counterparty default - total	R0330	-	-
Technical provisions minus recoverables from reinsurance/SPV and finite re - total	R0340	-	-



## S.17.01.02

## Non-life technical provisions

<b>Technical provisions calculated as a whole</b>	R0010
Total recoverables from reinsurance/SPV and finite re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole	R0050
<b>Technical provisions calculated as a sum of BE and RM</b>	
Best estimate	
Premium provisions	
Gross	R0060
Total recoverable from reinsurance/SPV and finite re after the adjustment for expected losses due to counterparty default	R0140
Net best estimate of premium provisions	R0150
<b>Claims provisions</b>	
Gross	R0160
Total recoverable from reinsurance/SPV and finite re after the adjustment for expected losses due to counterparty default	R0240
<b>Net best estimate of claims provisions</b>	R0250
<b>Total best estimate – gross</b>	R0260
<b>Total best estimate – net</b>	R0270
<b>Risk margin</b>	R0280
<b>Amount of the transitional on technical provisions</b>	
Technical provisions calculated as a whole	R0290
Best estimate	R0300
Risk margin	R0310
<b>Technical provisions – total</b>	
Technical provisions – total	R0320
Recoverable from reinsurance contract/SPV and finite re after the adjustment for expected losses due to counterparty default – total	R0330
Technical provisions minus recoverables from reinsurance/SPV and finite re – total	R0340

Legal expenses insurance	Direct business and accepted proportional reinsurance			Accepted non-proportional reinsurance			Total non-life obligation
	Assistance	Miscellaneous financial loss	Non-proportional health reinsurance	Non-proportional casualty reinsurance	Non-proportional marine, aviation and transport reinsurance	Non-proportional property reinsurance	
C0110	C0120	C0130	C0140	C0150	C0160	C0170	C0180
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
146,800	-4,163	9,707	-	-	-	-	152,343
0	0	0	-	-	-	-	0
146,800	-4,163	9,707	-	-	-	-	152,343
806,985	5,401	3,072	-	-	-	-	815,458
0	0	0	-	-	-	-	0
<b>806,985</b>	<b>5,401</b>	<b>3,072</b>	-	-	-	-	<b>815,458</b>
<b>953,785</b>	<b>1,238</b>	<b>12,778</b>	-	-	-	-	<b>967,801</b>
<b>953,785</b>	<b>1,238</b>	<b>12,778</b>	-	-	-	-	<b>967,801</b>
<b>28,122</b>	<b>188</b>	<b>107</b>	-	-	-	-	<b>28,418</b>
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
981,907	1,426	12,885	-	-	-	-	996,219
0	0	0	-	-	-	-	0
981,907	1,426	12,885	-	-	-	-	996,219

## S.19.01.21

## Non-life insurance claims

**Total non-life business**

Accident year/Underwriting year	Z0010	Accident year
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**Gross claims paid (non-cumulative)***(absolute amount)*

		Development year					
Year		0	1	2	3	4	5
		C0010	C0020	C0030	C0040	C0050	C0060
Prior	R0100	-	-	-	-	-	-
N-9	R0160	84,708	94,242	42,818	26,902	18,285	12,791
N-8	R0170	94,240	94,246	42,217	25,490	16,558	10,972
N-7	R0180	95,673	94,328	40,314	24,638	17,621	11,154
N-6	R0190	99,655	86,591	39,069	24,517	15,512	10,715
N-5	R0200	97,981	86,173	41,236	23,483	15,388	9,580
N-4	R0210	99,134	92,856	39,509	22,259	14,803	
N-3	R0220	108,602	93,627	40,051	22,710		
N-2	R0230	119,104	99,278	41,946			
N-1	R0240	131,948	103,484				
N	R0250	140,906					

**Gross undiscounted best estimate claims provisions***(absolute amount)*

		Development year					
Year		0	1	2	3	4	5
		C0200	C0210	C0220	C0230	C0240	C0250
Prior	R0100	-	-	-	-	-	-
N-9	R0160	0	0	0	0	0	0
N-8	R0170	0	0	0	0	0	0
N-7	R0180	0	0	0	0	0	0
N-6	R0190	0	0	0	0	0	0
N-5	R0200	0	0	0	0	0	33,242
N-4	R0210	0	0	0	0	44,110	
N-3	R0220	0	0	0	63,929		
N-2	R0230	0	0	92,062			
N-1	R0240	0	144,235				
N	R0250	258,128					

Development year					In current year	Sum of years (cumulative)
6	7	8	9	10 & +		
C0070	C0080	C0090	C0100	C0110	C0170	C0180
-	-	-	-	2,426	R0100	2,426
8,921	6,467	4,238	2,836		R0160	2,836
7,470	5,195	3,264			R0170	3,264
7,202	5,370				R0180	5,370
7,120					R0190	7,120
					R0200	9,580
					R0210	14,803
					R0220	22,710
					R0230	41,946
					R0240	103,484
					R0250	140,906
				<b>Total</b>	R0260	<b>361,493</b>
						<b>4,123,356</b>

Development year					Year end (discounted data)	
6	7	8	9	10 & +		
C0260	C0270	C0280	C0290	C0300	C0360	
-	-	-	-	3,695	R0100	3,607
0	0	0	11,881		R0160	11,624
0	0	13,986			R0170	13,685
0	19,734				R0180	19,370
25,699					R0190	25,271
					R0200	32,616
					R0210	41,903
					R0220	63,015
					R0230	90,886
					R0240	142,675
					R0250	256,163
				<b>Total</b>	R0260	<b>733,728</b>

**S.23.01.01****Own funds****Basic own funds before deduction for participations in other financial sectors as foreseen in article 68 of Delegated Regulation (EU) 2015/35**

Ordinary share capital (gross of own shares)	
Share premium account related to ordinary share capital	
Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings	
Subordinated mutual member accounts	
Surplus funds	
Preference shares	
Share premium account related to preference shares	
Reconciliation reserve	
Subordinated liabilities	
An amount equal to the value of net deferred tax assets	
Other own fund items approved by the supervisory authority as basic own funds not specified above	

**Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds**

Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds	
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**Deductions**

Deductions for participations in financial and credit institutions	
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**Total basic own funds after deductions****Ancillary own funds**

Unpaid and uncalled ordinary share capital callable on demand	
Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual-type undertakings, callable on demand	
Unpaid and uncalled preference shares callable on demand	
A legally binding commitment to subscribe and pay for subordinated liabilities on demand	
Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	
Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	
Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	
Supplementary members calls – other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	
Other ancillary own funds	

**Total ancillary own funds****Available and eligible own funds**

Total available own funds to meet the SCR	
Total available own funds to meet the MCR	
Total eligible own funds to meet the SCR	
Total eligible own funds to meet the MCR	

**SCR****MCR****Ratio of eligible own funds to SCR****Ratio of eligible own funds to MCR****Reconciliation reserve**

Excess of assets over liabilities	
Own shares (held directly and indirectly)	
Foreseeable dividends, distributions and charges	
Other basic own fund items	
Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	

**Reconciliation reserve****Expected profits**

Expected profits included in future premiums (EPIFP) – life business	
Expected profits included in future premiums (EPIFP) – non-life business	

**Total expected profits included in future premiums (EPIFP)**

	Total	Tier 1 – unrestricted	Tier 1 – restricted	Tier 2	Tier 3
	C0010	C0020	C0030	C0040	C0050
	-	-	-	-	-
R0010	100,000	100,000	-	0	0
R0030	0	-	-	0	0
R0040	-	-	-	-	0
R0050	-	-	-	-	-
R0070	-	-	-	0	0
R0090	-	-	-	-	-
R0110	-	-	-	-	-
R0130	1,042,266	1,042,266	-	0	0
R0140	32,601	0	-	32,601	0
R0160	0	0	-	0	0
R0180	-	-	-	-	-
	-	-	-	-	-
R0220	0	-	-	-	-
	-	-	-	-	-
R0230	0	0	0	0	0
R0290	<b>1,174,866</b>	<b>1,142,266</b>	<b>0</b>	<b>32,601</b>	<b>0</b>
	-	-	-	-	-
R0300	-	-	-	-	-
	-	-	-	-	-
R0310	-	-	-	-	-
R0320	-	-	-	-	-
R0330	-	-	-	-	-
R0340	-	-	-	-	-
R0350	-	-	-	-	-
R0360	-	-	-	-	-
R0370	-	-	-	-	-
R0390	-	-	-	-	-
R0400	-	<b>0</b>	<b>0</b>	-	-
	-	-	-	-	-
R0500	1,174,866	1,142,266	0	32,601	0
R0510	1,174,866	1,142,266	0	32,601	0
R0540	1,174,866	1,142,266	0	32,601	0
R0550	1,174,317	1,142,266	0	32,051	0
R0580	<b>356,125</b>	-	-	-	-
R0600	<b>160,256</b>	-	-	-	-
R0620	<b>3.30</b>	-	-	-	-
R0640	<b>7.33</b>	-	-	-	-
	-	-	-	-	-
	<b>C0060</b>				
R0700	1,162,266				
R0710	0				
R0720	20,000				
R0730	100,000				
R0740	0				
R0760	<b>1,042,266</b>				
	-				
R0770	-70,983				
R0780					
R0790	<b>-70,983</b>				

## S.25.02.21

## Solvency capital requirement – for undertakings using the standard formula and partial internal model

Unique number of component	Component description	Calculation of the solvency capital requirement	Amount modeled	USP	Simplifications
C0010	C0020	C0030	C0070	C0080	C0090
1	Market risk	313,983	313,983		
2	Counter-party default risk	13,638	13,638		
3	Life underwriting risk	0			
4	Health underwriting risk	0			
5	Non-life underwriting risk	158,005	158,005		
6	Intangible asset risk	0			
7	Operational risk	28,914			
8	LAC technical provisions	0			
9	LAC deferred taxes	-63,735			
<b>Calculation of solvency capital requirement</b>		<b>C0100</b>			
	Total undiversified components	R0110	450,806		
	Diversification	R0060	-94,681		
	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	R0160	0		
	<b>Solvency capital requirement excluding capital add-on</b>	<b>R0200</b>	<b>356,125</b>		
	Capital add-ons already set	R0210	0		
	<b>Solvency capital requirement</b>	<b>R0220</b>	<b>356,125</b>		
	<b>Other information on SCR</b>		-		
	Amount/estimate of the overall loss-absorbing capacity of technical provisions	R0300	0		
	Amount/estimate of the overall loss-absorbing capacity of deferred taxes	R0310	0		
	Capital requirement for duration-based equity risk sub-module	R0400	0		
	Total amount of notional solvency capital requirements for remaining part	R0410	0		
	Total amount of notional solvency capital requirements for ring fenced funds (other than those related to business operated in accordance with Art. 4 of Directive 2003/41/EC (transitional))	R0420	0		
	Total amount of notional solvency capital requirement for matching adjustment portfolios	R0430	0		
	Diversification effects due to RFF nSCR aggregation for article 304	R0440	0		

## S.28.01.01

## Minimum capital requirement – only life or only non-life insurance or reinsurance activity

**Linear formula component for non-life insurance and reinsurance obligations**

C0010		
MCRNL result	R0010	170,143

			Net (of reinsurance/SPV) best estimate and TP calculated as a whole C0020	Net (of reinsurance) written premiums in the last 12 months C0030
Medical expense insurance and proportional reinsurance		R0020	-	-
Income protection insurance and proportional reinsurance		R0030	-	-
Workers' compensation insurance and proportional reinsurance		R0040	-	-
Motor vehicle liability insurance and proportional reinsurance		R0050	-	-
Other motor insurance and proportional reinsurance		R0060	-	-
Marine, aviation and transport insurance and proportional reinsurance		R0070	-	-
Fire and other damage to property insurance and proportional reinsurance		R0080	-	-
General liability insurance and proportional reinsurance		R0090	-	-
Credit and suretyship insurance and proportional reinsurance		R0100	-	-
Legal expenses insurance and proportional reinsurance		R0110	953,086	797,741
Assistance and proportional reinsurance		R0120	1,238	47,157
Miscellaneous financial loss insurance and proportional reinsurance		R0130	12,778	26,050
Non-proportional health reinsurance		R0140	-	-
Non-proportional casualty reinsurance		R0150	-	-
Non-proportional marine, aviation and transport reinsurance		R0160	-	-
Non-proportional property reinsurance		R0170	-	-

## S.28.01.01

## Minimum capital requirement – only life or only non-life insurance or reinsurance activity

## Linear formula component for life insurance and reinsurance obligations

		<b>C0040</b>
MCRL result	R0200	-

				Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk
				C0050	C0060
Obligations with profit participation – guaranteed benefits		R0210		-	-
Obligations with profit participation – future discretionary benefits		R0220		-	-
Index-linked and unit-linked insurance obligations		R0230		-	-
Other life (re)insurance and health (re)insurance obligations		R0240		-	-
Total capital at risk for all life (re)insurance obligations		R0250		-	-

## Overall MCR calculation

		<b>C0070</b>
Linear MCR	R0300	170,143
SCR	R0310	356,125
MCR cap	R0320	160,256
MCR floor	R0330	89,031
Combined MCR	R0340	160,256
Absolute floor of the MCR	R0350	2,500
		<b>C0070</b>
Minimum capital requirement	R0400	160,256

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

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

## Credits

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