Annual Report 2017

SOVAG
Schwarzmeer und Ostsee
Versicherungs-Aktiengesellschaft
Hohe Bleichen 11
20354 Hamburg

District Court of Hamburg
HRB 3560

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Contents

Please note:
Discrepancies may appear in the tables and reports as a result of rounding.

The present document is an unofficial translation for information purposes only. If there is a discrepancy between the English translation and the German original, the German version shall prevail.

Report of the Supervisory Board

In fulfilment of its responsibilities, the Supervisory Board continued to maintain an Audit Committee and a Human Resources Committee throughout 2017, which consulted on a regular basis. The Audit Committee was engaged, in particular, with the monitoring of the accounting and bookkeeping of the company, as well as ensuring the effectiveness of internal controlling systems, the risk management system, compliance organisation and internal auditing. In the course of 2017, the Human Resources Committee occupied itself with various issues relating to the Management Board as well as the substantial workforce downsizing that was undertaken as of mid-2017.

The Supervisory Board and its committees oversaw the management of the company's business on a continuous basis and provided advisory guidance on ongoing and discrete matters. In total, the Supervisory Board convened for eight extended meetings and also held regular discussions with management, especially in support of the appointment of the new Management Board in April 2017. With regard to the difficult financial situation of the company in the first three quarters of 2017, the Supervisory Board responded to advice from outside counsel and the encouragement of the company's regulator, BaFin, by intensifying its monitoring of liquidity, solvency and claims management matters.

The Supervisory Board was closely involved in, and accompanied, the major decisions on the company's strategic repositioning and restructuring. Of note here were:

- decisions involving obtaining additional capital to ensure financial stability
- the replacement of the company's Management Board
- the termination of substantial numbers of company employees
- the closing of the company's London branch
- ongoing asset and capital management measures, especially in connection with the restructuring and repositioning of the company's business
- cessation of new business and wind-down of the company's insurance contracts (throughout 2017 and with urgency as of Q2 upon the appointment of the new Management Board)
- the negotiation and signing of commutation agreements
- the process to obtain an acquirer to sell the company's primary insurance portfolio

The Supervisory Board additionally advised on and consulted intensively with management in respect of SCR issues.

Finally, the Supervisory Board monitored management discussions and negotiations with the company's regulator, BaFin, including inviting representatives of BaFin to attend one of its meetings.The Supervisory Board was informed regularly and comprehensively by the company's Management Board on all matters relating to the company's business and its strategic repositioning.

During its eight proper meetings in 2017, the Supervisory Board extensively discussed the financial development of the company and its revenues and risk exposure, the development and maintenance of appropriate insurance reserves for claims and risks, as well as reinsurance ratios and terms, and the risk and liquidity management of the company as a whole. The results of Supervisory Board meetings were recorded in comprehensive minutes which were distributed and discussed among the Supervisory Board members and ultimately approved in the context of subsequent meetings. In between meetings, resolutions were passed via circular written resolutions and the Supervisory Board was kept informed of essential matters via email, financial reporting and orally.

The Supervisory Board is presently one member short after the resignation of member Michael Gerlach (employee representative) in Q4 2017. A replacement member has yet to be elected.

In its meeting on 19 May 2017, the Supervisory Board appointed PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Hamburg (PwC) as the auditor of the company for the 2017 business year pursuant to § 341 k of the German Commercial Code (HGB). The company's accounting, annual financial statements and management reporting for the 2017 business year were accordingly audited by PwC. The audit has established no grounds to object to the accounting, financial statements and management reporting; an audit certification without qualifications was issued. The report prepared by the Management Board on the company's relationships with affiliated businesses (pursuant to § 312 AktG) was likewise reviewed by PwC and was issued with an audit certification without qualifications. The auditor's report was provided to all of the members of the Supervisory Board immediately. Representatives of the auditor attended the meeting to adopt the annual financial statements held on 20 April 2018. In addition to the reports provided, the results of the audit were also discussed in detail orally and questions posed by the members of the Supervisory Board were answered. The Supervisory Board acknowledged the audit reports and the additional supplementary explanations of the auditor with approval.

Having concluded its review, the Supervisory Board has no objections to the Company's 2017 annual financial statements, along with the report on the company's business affairs (Lagebericht) and the report of the Management Board on the company's relationships to affiliated business, each of which were prepared as of 31 December 2017. The Supervisory Board concurs with the opinion taken by the auditor and approves the annual financial statements prepared by the Management Board, which are accordingly adopted in accordance with § 172 AktG.

The Supervisory Board thanks all of the employees of the company and the Management Board for their consistent efforts and hard work under extremely difficult circumstances over the past year.

Hamburg, May 2018

Chlodwig Reuter
Chairman of the Supervisory Board

Management

SUPERVISORY BOARD

Chlodwig Reuter
Chairman
Chairman of the Board, VOLGA Resources Investments S.A.,
Luxembourg

Dmitry Talaev
Deputy Chairman
Member of the Board of SOGAZ Insurance,
Moscow

Alexey Leonenko
Deputy Chairman of the Board of SOGAZ Insurance,
Moscow

Tatyana Pereyma
Advisor of General Director, Gazprom Export LLC,
St. Petersburg

Thomas Oliver Scheibel
Independent Supervisory Board member,
Geneva

Oleg Tarasov
Deputy Head of Directorate, Legal Department at PJSC Gazprom,
Moscow

Stefan Gerlach*
Former employee, SOVAG,
Wentorf near Hamburg, until 31 December 2017

Christian Illgner*
Head of Accounting, SOVAG,
Müssen

Heidemarie Küch*
Former employee, SOVAG,
Dohren

*Employee representative.

MANAGEMENT BOARD

Arndt Gossmann
Chairman of the Management Board,
Hamburg, since 1 May 2017

Dr Harald Gerd Meyer
Member of the Management Board,
Keitum, since 1 May 2017

Michel Schade
Chairman of the Management Board,
Hamburg, until 30 April 2017

Alexander Jeßnitzer
Member of the Management Board,
Hamburg, until 30 April 2017

Management Report

Management Report

BUSINESS ACTIVITIES AND GENERAL CONDITIONS

Business model

Founded in 1927, Schwarzmeer und Ostsee Versicherungs-Aktiengesellschaft SOVAG is an insurance company with registered office in Hamburg, Germany.

In light of SOVAG's continued unsatisfactory economic performance, the management bodies initiated a comprehensive strategic restructuring process. The measures involved are commensurate with the difficult situation, as well as with the responsibility towards shareholders, partners, employees and, not least, policyholders. Against this background, the decision was taken to discontinue SOVAG's ongoing operating business and to withdraw from the market.

SOVAG's business activity spanned both primary insurance and reinsurance. The company's insurance programme included all significant composite insurer lines of business such as motor, third-party liability, accident and transport insurance and all significant property lines. Sales were made primarily through national and international brokers. SOVAG operated a branch in London in the financial year.

Shareholder structure and legal background

GAZPROM Germania GmbH (GPG), Berlin, holds 50.1% of the shares in SOVAG. INSURANCE COMPANY OF GAZ INDUSTRY SOGAZ (SOGAZ), Moscow, holds 25.1%, and VOLGA Resources Investments S.A. (VOLGA), Luxembourg, 24.8%. The majority shareholder, GPG, is in turn a fully-owned subsidiary of Gazprom Export, St. Petersburg, and (indirectly) of PJSC Gazprom, Moscow.

In accordance with International Financial Reporting Standards (IFRSs), SOVAG is included in the consolidated financial statements SOGAZ and in the (sub-)group financial statements of GPG, using the equity method in each case.

SOVAG also prepares separate financial statements in accordance with German Generally Accepted Accounting Principles as provided for the German Commercial Code [Handelsgesetzbuch – HGB] and the German Accounting Regulations for Insurance Companies [Verordnung über die Rechnungslegung von Versicherungsunternehmen – RechVersV].

Significant events

In December 2016, the SOVAG Management Board, in coordination with the Supervisory Board, passed a resolution to suspend all of the company's ongoing business, and since June 2017 it has not underwritten any new business. All insurance contracts concluded directly with SOVAG have been proactively terminated to their due date or are not being renewed on expiry.

In February 2017, the company's share capital was strengthened by a contribution of EUR 10 million paid in by its shareholders, and with the appointment of a new Management Board in May a fundamental restructuring process was initiated. This process should be completed by August 2018.

The central aim of the restructuring process initiated by the new board was to neutralise insurance risks resulting from the company's previous business, modify the operational structure and reduce costs.

The key restructuring measures introduced include:

- stabilising the company economically
- fulfilling supervisory requirements
- implementing the resolution passed in December 2016 and bring forward the suspension of new business
- identifying and contracting a risk carrier for complete insurance portfolio transfer
- settlement of reinsurance relationships
- adjusting the business organisation and personnel structure

On 31 December 2017, agreement was reached on the transfer of all actuarial reserves to a risk carrier specialised in run-off pursuant to Section 13 of the German Act on the Supervision of Insurance Undertakings [Versicherungsaufsichtsgesetz – VAG]. Subject to approval by the Federal Financial Supervisory Authority [BaFin], closing of the portfolio transfer agreement is expected for Q2 2018. To this end, a commutation agreement with SOGAZ as SOVAG's major reinsurer was concluded on 3 November 2017. Implementation of the agreement is linked to the closing of the portfolio transfer.

Relationships with sales partners are being properly terminated and transferred to the purchaser of the portfolio. Insurance policies existing beyond 31 December 2017 have primarily been rolled over or terminated by mutual agreement. Insurance policies due to expire after 1 January 2018 will be transferred to an alternative risk carrier under the portfolio transfer agreement.

In order to obtain a sound representation of the company and create an effective basis for planning, extensive reviews were performed in the course of the restructuring process. Among other things, these revealed that the reinsurer SOGAZ no longer met the minimum rating requirements of two confirmed investment grade ratings from accepted rating agencies. Consequently, the continued reinsurance coverage under German commercial law was no longer recognised in the solvency statement. Hence, at the end of Q2, the prescribed SCR coverage ratio was not quite reached. Following an adjustment of SOGAZ' rating by Standard & Poor's, an adequate SCR coverage ratio was re-established in Q3 2017.

On 30 August 2017, the Management Board and the works council agreed on a reconciliation of interests and a social plan. As a result, by the end of the restructuring phase the employee base will probably comprise 17 employees.

SOVAG's B+ rating, which has been under review, was reassessed and confirmed by A.M. Best in March. As it has suspended all underwriting activity, SOVAG decided to withdraw from the rating process. The final rating in October 2017 once again confirmed the B+ rating.

Our employees

At the end of 2017, SOVAG employed a total of 29 members of staff (end of 2016: 74). Of these, 28 members of staff were employed in Germany and one in London. Three staff members are employed on a part-time basis. A further 12 left the company with effect from 1 January 2018.

Association memberships

SOVAG is a member of the German Insurance Association [Gesamtverband der Deutschen Versicherungswirtschaft e.V.], of the Association for Assisting Traffic Accident Victims [Verein Verkehrsopferhilfe e.V.] as well as of the Eastern and Central European Association [Ost- und Mitteleuropaverein e.V.]. SOVAG is a guest member of the Employer's Federation of the Insurance Companies in Germany [Arbeitgeberverband der Versicherungsunternehmen in Deutschland e.V.].

Macroeconomic development

On the whole, compared with 2016, the global economy gained in breadth in 2017. International organisations are currently expecting almost all major national economies to post appreciable growth for the 2017 calendar year. Among the industrialised nations, economic activity in the US and the euro zone developed with unexpected dynamism, with a higher rate of growth than in the previous year. Spain, in particular, recorded strong gross domestic product (GDP) growth, while in France and Italy economic activity is in the meantime also on a clear upward path. Against the background of Brexit, growth in the UK was rather more moderate. In the commodity-exporting emerging economies, rising raw material prices once again strengthened business activity.

In its most recently published economic forecasts, the International Monetary Fund (IMF) estimates that global economic growth in 2017 increased from the projected 3.2% to 3.7%. For the euro zone, growth in economic output is put at 2.4%.

According to the Federal Statistical Office, in Germany gross domestic product in real terms was up by a solid 2.2% based on the year as a whole.

Development on the capital markets

The improved general economic outlook also had a positive effect on the financial markets in the past few months. For equity investors in particular, 2017 was a gratifying year. Corporate profits rose strongly in line with the recovery of the global economy and some stock indices recorded new highs in the course of the year. The most important stock market index for the euro zone, the Euro Stoxx 50 (price index), increased in the reporting period from 3,290 to 3,504 points, a rise of 6.5%. The German stock index DAX (performance index) increased by 12.5% from 11,481 to 12,917 points.

The development on the bond markets was, by contrast, again influenced by monetary policy. Worldwide, interest rates developed inconsistently, however. Of the central banks, so far only the Fed has taken steps towards returning to normal rates by raising the base rate and reducing total assets. In the euro zone, the base rate remained unchanged at 0.0%. The deposit rate was –0.4%. The interest rate for the so-called marginal lending facility, which allows eligible institutions in the euro zone to borrow money from the European Central Bank (ECB) on a short-term basis, was set at 0.25%.

Positive economic data for the euro zone caused the euro to rise appreciably from spring onwards. Moreover, changed expectations in relation to economic policy stimuli in the USA are likely to have additionally supported the single European currency against the US dollar over the summer, resulting in a steady rise of the euro exchange rate versus the US dollar in the course of 2017. Most recently, it was quoted at USD 1.20, approximately 13.5% higher than the exchange rate as at 31 December 2016.

Development of the German insurance market

Property and accident insurance show sustained demand due to their indispensable role in providing coverage for different private, commercial and industrial risks.

Based on the quarterly figures presented by the composite insurance enterprises for Q3, the German Insurance Association [Gesamtverband der Deutschen Versicherungswirtschaft e.V.] is expecting stable premium growth of 2.9% overall for 2017 as a whole, with above-average positive growth rates especially for homeowners, motor and legal protection insurance lines.

DEVELOPMENTS AT SOVAG

Overview

The restructuring measures ongoing since May 2017 characterise SOVAG's financial performance.

The net technical result improved from EUR –11.5 million in 2016 to EUR –1.8 million.

The total costs of personnel and material expenses in the amount of EUR 18.1 million (2016: EUR 17.2 million) is slightly higher than the previous year's level and contains all significant restructuring costs. This item includes one-off effects of EUR 4.7 million, principally for consultancy services and severance payments.

The loss for the year decreased from EUR 14.9 million in 2016 to EUR 11.1 million. After a contribution to capital reserves of EUR 10 million paid in by the company's shareholders, equity was at EUR 14.3 million compared with EUR 15.4 million in 2016.

Premium development

Gross premiums written amounted to EUR 36.0 million in the 2017 reporting period, which is EUR 17.0 million, or 32.0%, below the comparable figure for 2016. This is primarily due to the discontinuation of new underwriting business and the termination or rollover of existing insurance contracts. In direct insurance business, gross premiums written fell by 26.0%, or EUR 9.5 million, while in inward reinsurance the decline amounted to 45.6%, or EUR 7.5 million. In outward reinsurance, a total of EUR 20.2 million (2016: EUR 26.8 million) in premiums was ceded to reinsurers, representing a reinsurance ratio of 56.0% (2016: 50.5%). Net premiums written thus amounted to EUR 15.8 million (2016: EUR 26.2 million).

Claims incurred

Gross expenditure for claims during the financial year declined by EUR 24.6 million, or 35.8%, compared with the previous year to EUR 44.1 million. A gain of EUR 8.0 million (2016: EUR 3.5 million) was recorded for the settlement of provisions for prior-year claims. Overall, the gross expenditure for claims fell to EUR 36.1 million, a decline of EUR 29.2 million, or 44.7%. The gross total claims ratio thus decreased from 117.0% to 83.2%. The proportion of reinsurers in the overall claims expenditure amounted to EUR 23.9 million (2016: EUR 44.9 million). Total net loss expenses came to EUR 12.2 million (2016: EUR 20.4 million). This corresponds to a net total claims ratio of 64.0% (2016: 72.4%).

Costs

Gross expenses for insurance operations fell by EUR 6.4 million to EUR 14.0 million. The gross cost ratio decreased from 36.5% to 32.3%. SOVAG received EUR 2.9 million in commissions from reinsurers (2016: EUR 3.1 million). Net expenses for insurance operations thus amounted to EUR 11.1 million (2016: EUR 17.2 million). Overall, the net cost ratio decreased year-on-year from 61.2% to 58.1%.

The combined ratio (combined ratio of loss and cost to net premiums earned) fell to 122.1% in spite of the declining premium income (2016: 133.6%).

Technical result

The gross technical result (prior to changes in the equalisation reserve and similar provisions) closed with a loss of EUR 5.6 million (2016: loss of EUR 29.2 million).

From its outward reinsurance business, the company recorded income of EUR 2.4 million (2016: EUR 20.7 million). Thus the net technical result prior to changes in the equalisation reserve and similar provisions closed with a loss of EUR 3.2 million (2016: EUR 8.5 million).

A net amount of EUR 0.1 million was taken from the equalisation reserve in the financial year 2017 (2016: allocation of EUR 3.1 million). The nuclear installation provision ("similar" provisions) was reversed. Following changes in the equalisation reserve and similar provisions, the net technical result recorded a loss of EUR 1.8 million (2016: loss of EUR 11.5 million).

Non-technical result

The non-technical result in the amount of EUR – 9.6 million (2016: EUR – 3.6 million) was composed of investment income of EUR 1.0 million (2016: EUR 3.3 million) and other comprehensive income (balance of other income and expenses). The lower investment income is determined with EUR 1.4 million by a one-off effect from the sale of real estate in 2016. In other comprehensive income, a loss of EUR 10.6 million (2016: loss of EUR 6.9 million) was recognised, whereby the deterioration is principally due to (one-off) expenses in connection with the restructuring measures.

The proportional raising of pension provisions as a result of the first-time application of the German Accounting Law Modernisation Act (BilMoG) resulted in extraordinary expense in the amount of EUR 0.1 million.

Overall, SOVAG recognised a pre-tax loss of EUR 11.5 million in the financial year 2017 (2016: loss of EUR 15.3 million).

An income tax expense of EUR 0.2 million was determined as a result of a tax audit carried out in the reporting period (2016: tax rebate of EUR 0.2 million). Together with anticipated VAT refunds of EUR 0.6 million, this resulted in tax income totalling EUR 0.4 million (2016: EUR 0.4 million) for the reporting period.

Thus the company closed the financial year with a net loss for the year after taxes of EUR 11.1 million (2016: EUR 14.9 million).

In summary, the overall result for the reporting period presents as follows:

in EUR thousands	2017	2016
Technical result for own account prior to changes in the equalisation reserve and similar provisions	**– 3,206**	**– 8,470**
Changes in the equalisation reserve and similar provisions	– 1,405	3,074
Technical result for own account	**– 1,801**	**– 11,544**
Non-technical income from ordinary activities	3,928	7,051
Non-technical expenses from ordinary activities	13,551	10,699
Non-technical result from ordinary activities	**– 9,622**	**– 3,648**
Extraordinary income	0	0
Extraordinary expenses	101	101
Extraordinary result	**– 101**	**– 101**
Earnings before taxes	**– 11,524**	**– 15,293**
Taxes	– 417	– 390
Net loss for the financial year	**– 11,107**	**– 14,903**
Retained profits/accumulated losses brought forward	– 14,903	0
Net accumulated losses (–)	**– 26,010**	**– 14,903**

BUSINESS PERFORMANCE BY LINES OF BUSINESS

Measured by gross premiums written of EUR 36,016 thousand (2016: EUR 52,988 thousand), the insurance portfolio is made up as follows:

in %	2017	2016
Direct insurance business (excluding fronting)	**73.0**	**81.7**
Liability insurance	5.7	7.7
Third-party motor insurance	19.5	17.6
Other motor insurance	4.4	3.9
Fire and property insurance	16.4	31.0
comprising:		
Fire insurance	4.9	6.2
Comprehensive homeowner’s insurance	4.3	15.0
Other property insurance	7.2	9.8
Transport insurance	15.7	10.4
Other insurance classes	11.3	11.1
Fronting	**11.3**	**– 4.0**
Inward reinsurance business (excluding fronting)	**15.7**	**22.3**

The number of contract coverages in direct insurance business fell by 135,781 to 138,281 in the 2017 financial year.

PERFORMANCE OF DIRECT INSURANCE BUSINESS

Liability insurance

Gross premiums earned in the liability insurance line of business decreased by 44.9% to EUR 2,362 thousand. Of this amount, EUR 0 thousand (2016: EUR 29 thousand) related to fronting business. Supplementary premiums worth EUR 166 thousand are brought into account in years after they were written.

With claims expenditure for the financial year standing at EUR 2,304 thousand and run-off profits at EUR 1,175 thousand, a gross claims ratio of 47.8% was posted for 2017, which was lower than the previous year's value (2016: 57.0%).

Gross expense for insurance operations stood at EUR 1,248 thousand, 35.5% lower than in the previous year.

Prior to changes in the equalisation reserve, the gross technical result improved from a loss of EUR 162 thousand in the previous year to a profit of EUR 62 thousand. Following reinsurance expenses of EUR 214 thousand (2016: EUR 230 thousand) and factoring in an allocation to the equalisation reserve of EUR 497 thousand (2016: EUR 516 thousand), this line of business closed with a technical loss for own account in the amount of EUR 649 thousand (2016: loss of EUR 908 thousand).

Third-party motor insurance

In the third-party motor insurance segment, gross premiums earned decreased by EUR 1,293 thousand, or 13.5% to EUR 8,293 thousand.

Claims expenses for the financial year increased year-on-year by 29.2% to EUR 9,998 thousand. Settlement gains of EUR 3,286 thousand were recognised in the outstanding claims reserve carried forward. As a result, the gross claims ratio for the reporting period increased to 80.9% (2016: 69.4%). The gross cost ratio decreased from 21.4% to 18.0%.

Prior to changes in the equalisation reserve, a gross underwriting profit was recognised in the amount of EUR 229 thousand (2016: EUR 1,135 thousand). Following reinsurance expense of EUR 1,093 thousand (2016: income of EUR 1,967 thousand) and a withdrawal from the equalisation reserve amounting to EUR 376 thousand (2016: an allocation of EUR 4,367 thousand), this business line closed with a net underwriting loss of EUR 488 thousand (2016: loss of EUR 1,265 thousand).

Other motor insurance

Gross premiums earned for the risk classes in this line of business decreased by EUR 42 thousand, or 2.3%, to EUR 1,801 thousand.

Claims expenses fell by 17.1% to EUR 947 thousand. This includes EUR 378 thousand in run-off profits for insured events from prior periods (2016: EUR 279 thousand). As a result, a reduced claims ratio year-on-year of 52.6% was recorded at 31 December 2017 (2016: 62.0%).

The gross cost ratio was 18.8% (2016: 24.4%).

A gross underwriting profit was recognised in the amount of EUR 618 thousand (2016: EUR 253 thousand) prior to changes in the equalisation reserve. Following reinsurance expenses of EUR 476 thousand (2016: EUR 79 thousand) and an allocation to the equalisation reserve of EUR 332 thousand (2016: EUR 582 thousand), this line of business closed with a technical loss for own account of EUR 189 thousand (2016: loss of EUR 407 thousand).

Transport insurance

In transport insurance, gross premiums earned in 2017 increased by 2.4% from EUR 5,530 thousand to EUR 5,661 thousand, of which EUR 1,588 thousand relates to supplementary premiums brought into account in years after they were written.

Expenses for insured claims increased by 25.4% to EUR 3,042 thousand. This led to an increased claims ratio year-on-year of 53.7% (2016: 43.9%). Income totalling EUR 1,405 thousand (2016: EUR 3,430 thousand) relates to settlement of prior-year claims.

Gross expenses for insurance operations increased during the year ended 31 December 2017 by 33.7% to EUR 2,215 thousand.

Prior to changes in the equalisation reserve, a gross profit was recognised in the amount of EUR 436 thousand (2016: EUR 1,481 thousand). After factoring in income from reinsurance with EUR 2,064 thousand (2016: expense of EUR 953 thousand) and an allocation to the equalisation reserve of EUR 3,393 thousand (2016: EUR 1,178 thousand), this business line closed with a loss for own account of EUR 892 thousand (2016: loss of EUR 649 thousand).

Fire insurance

In the fire insurance business line, gross premiums earned fell by 37.6% to EUR 2,058 thousand.

Claims expenses reduced overall by 41.2% to EUR 2,835 thousand. This item included run-off profits for insurance events from the prior period of EUR 880 thousand (2016: EUR 1,088 thousand). This led to a gross total claims ratio for 2017 of 137.7% (2016: 146.0%).

Gross expenses for insurance operations stood at EUR 1,236 thousand, which was 23.2% below the previous year's level.

Following a loss of EUR 3,023 thousand in the previous year, the gross technical result prior to changes in the equalisation reserve improved in the financial year ended 31 December 2017, with a loss of EUR 2,162 thousand being posted. Factoring in reinsurance income of EUR 909 thousand (2016: EUR 1,221 thousand) and a withdrawal from the equalisation reserve of EUR 195 thousand (2016: EUR 620 thousand), this business line closed with a net underwriting loss of EUR 1,058 thousand (2016: loss of EUR 1,182 thousand).

Comprehensive homeowner's insurance
Premiums earned in the comprehensive homeowner's insurance business line fell by 75.6% to EUR 1,956 thousand.

Compared with the previous year, total claims expenses declined by 65.2% to EUR 2,809 thousand, whereby settlement of prior-year provisions resulted in gains of EUR 211 thousand (2016: loss of EUR 248 thousand). As a result, a higher claims ratio year-on-year of 143.6% was recorded at 31 December 2017 (2016: 100.4%).

The gross cost ratio increased compared to the previous year from 48.3% to 44.8%.

At the end of the financial year 2017, a net underwriting loss of EUR 1,690 thousand (2016: loss of EUR 3,542 thousand) was recognised with unchanged equalisation reserve and reinsurance expenses of EUR 297 thousand (2016: EUR 113 thousand).

Other property insurance and other insurance classes
The insurance classes subsumed under this line of business include travel health, accident, comprehensive contents, burglary/theft and robbery, water damage, glass, storm, technical, extended coverage, business interruption insurance, aviation and other insurance classes, as well as travel assistance insurance.

Gross premiums earned increased by 50.4% overall from EUR 5,794 thousand to EUR 8,716 thousand. Fronting activities accounted for EUR 835 thousand in the financial year ended 31 December 2017 (2016: EUR –5,071 thousand). Premiums earned excluding fronting business amounted to EUR 7,881 thousand, which was 27.5% below the previous year's level.

With total claims expenses for the year of EUR 12,212 thousand and run-off losses of EUR 292 thousand (2016: run-off profits of EUR 1,422 thousand), this collective line of business recorded a gross claims ratio of 143.5% for 2017 (2016: 207.8%). Excluding fronting activities, the gross claims ratio reduced from 110.8% to 58.7%.

At EUR 3,052 thousand, gross expenses for insurance operations were 27.5% below the expenses for the previous year.

Prior to changes in the equalisation reserve, a gross underwriting loss of EUR 6,258 thousand was recognised (2016: EUR 10,621 thousand). After factoring in a withdrawal from the equalisation reserve in the amount of EUR 2,472 thousand (2016: EUR 1,193 thousand) and income from reinsurance of EUR 4,316 thousand (2016: income of EUR 6,506 thousand), this collective line of business closed with a net underwriting profit of EUR 529 thousand (2016: loss of EUR 2,922 thousand).

PERFORMANCE OF INWARD REINSURANCE BUSINESS

Assumed reinsurance business mainly focuses on the facultative assumption of insurance company risks. These premiums are written on the London market.

The largest share of indirect business, at 44.5% of gross premiums written, is in fire and property insurance (mainly fire and fire/BI), followed by other indemnity insurance at 36.1% and accident insurance at 16.9%.

Gross premiums earned across all lines of business came to EUR 12,484 thousand, 28.3% below the previous year's level (2016: EUR 17,411 thousand). Financial year claims expenses decreased from EUR 24,261 thousand to EUR 7,087 thousand. As a result of run-off profits arising from the outstanding claims reserve carried forward in the amount of EUR 1,001 thousand (2016: loss of EUR 3,394 thousand), a gross claims ratio of 48.8% was recognised for the year ended 31 December 2017 (2016: 158.8%).

Prior to changes in the equalisation reserve and similar provisions, a gross underwriting profit of EUR 2,883 thousand was recognised (2016: loss of EUR 14,795 thousand). Reinsurance expenses totalled EUR 2,829 thousand (2016: income of EUR 12,372 thousand). After factoring in a withdrawal from the equalisation reserve of EUR 1,317 thousand (2016: EUR 1,755 thousand) and the reduction of similar provisions in the amount of EUR 1,267 thousand (2016: EUR 0 thousand), a net underwriting profit of EUR 2,638 thousand was recognised (2016: loss of EUR 668 thousand).

SUMMARY APPRAISAL OF BUSINESS PERFORMANCE

With gross premiums written totalling EUR 36.0 million, the volume of premiums was 32.0% below the previous year's level of EUR 53.0 million in 2017. In view of the initiated restructuring measures and implementation of the decision to discontinue new underwriting business taken at the end of 2016 and implemented in May 2017, this development is in line with expectations.

Compared with the previous year, the claims ratio shown in the balance sheet decreased by 8.4 percentage points to 64.0%. The settlement of the outstanding claims reserve for prior-year claims resulted in a net profit for the financial year 2017 of EUR 8.0 million, following EUR 3.5 million in 2016.

At 58.1%, the net cost ratio was slightly lower than the previous year's level of 61.2%. The combined ratio stood at 122.1% (2016: 133.6%).

Direct insurance business recognised a gross underwriting loss prior to changes in the equalisation reserve totalling EUR 8.5 million, following a loss of EUR 14.4 million in the previous year. Of this amount, gross losses of EUR 7.1 million resulted from fronting activities (2016: loss of EUR 5.1 million).

Inward reinsurance business produced a gross underwriting profit prior to changes in the equalisation reserve and similar provisions of EUR 2.9 million (2016: loss of EUR 14.8 million).

Losses of the reinsurers amounted to EUR 2.4 million (2016: loss of EUR 20.7 million). Excluding fronting activities, this represents a profit for the reinsurers of EUR 4.5 million (2016: loss of EUR 18.4 million).

Overall, the net underwriting loss prior to changes in the equalisation reserve and similar provisions amounted to EUR 3.2 million (2016: loss of EUR 8.5 million). A negative – albeit significantly improved – underwriting performance was in line with expectations due to the restructuring plan.

The financial year 2017 closed with a net underwriting loss of EUR 1.8 million (2016: loss of EUR 11.5 million).

ASSETS AND FINANCIAL POSITION

Investments

Investments excluding deposits with ceding insurers from inward insurance business fell during the reporting period by EUR 22.3 million, or 23.1% to EUR 74.3 million. Deposits with ceding insurers from inward insurance business reduced during the same period by EUR 1.5 million to EUR 0.9 million. Total investment holdings thus decreased by 24.0% to EUR 75.1 million. Gross new assets achieved an overall volume of EUR 0.1 million (2016: EUR 31.8 million).

Holdings of land, land rights and buildings, including buildings on third-party land, decreased in line with depreciation by EUR 16 thousand in the reporting period. With a carrying amount of EUR 0.4 million, the proportion of investments excluding deposits with ceding insurers from inward reinsurance business accounted for 0.5% (2016: 0.4%).

Equity investments amounting to EUR 0.3 million were reclassified to other investment assets due to a revised holding intent. The relative proportion of total investments excluding deposits with ceding insurers from inward reinsurance business was 0.4% (2016: 0.3%).

The portfolio of shares, investment fund shares/units and other non-fixed-income securities decreased in the reporting period from EUR 33.8 million to EUR 33.3 million after factoring in write-downs and reversals of write-downs, which represents a proportion of investments excluding deposits with ceding insurers from inward reinsurance business of 44.8% (2016: 35.0%). Directly held shareholdings accounted for EUR 4.3 million, or 5.8% of the investment volume. Other equities relate to units in investment funds (primarily units in a special fund), which in turn are predominantly invested in bonds.

The portfolio of bearer bonds and other fixed-interest securities reduced during the reporting period by EUR 16.5 million to EUR 30.3 million after factoring in write-downs and reversals of write-downs in the amount of EUR 46.8 million. The relevant proportion of investments excluding deposits with ceding insurers from inward insurance business thus accounted for 40.8% (2016: 48.5%).

Other loans decreased in the reporting period by EUR 5.2 million to EUR 9.9 million. The proportion of investments excluding deposits with ceding insurers from inward reinsurance business corresponds to 13.3% (2016: 15.6%).

The calculation of the security and tied assets as at 31 December 2017 indicates surplus asset coverage.

Current regular investment income amounted to EUR 1.3 million in 2017. Less ordinary expenses of EUR 0.5 million (including depreciation on property), this produced a result from ordinary activities of EUR 0.8 million (2016: EUR 1.2 million). The decline in income is primarily explained by the fact that the profits from the special fund were retained and not distributed in 2017, as well as by the lower interest on the reinvestment.

At the balance sheet date, write-downs on SOVAG’s investments of EUR 0.6 million were recognised: conversely, income of EUR 0.2 million was posted from the reversal of impairment losses recognised in prior periods. Disposal gains of EUR 0.6 million were recognised in respect of the sale of assets. Thus, on balance this produced an (extraordinary) result of EUR 0.2 million (2016: EUR 2.1 million).

Net investment income thus decreased from EUR 3.3 million to EUR 1.0 million. In light of a continued low-risk investment policy and low interest rates, this result is within expectations. Current gross interest return on investments excluding deposits with ceding insurers from inward reinsurance business amounted to 1.6% in the financial year 2017 (2016: 20%). Net interest return fell from 3.5% to 1.2%.

In the period ended 31 December 2017, hidden net reserves decreased from EUR 4.8 million to EUR 3.9 million, with these hidden net reserves amounting to 5.3% of investments excluding deposits with ceding insurers from inward reinsurance business. Hidden net reserves can be broken down as follows: land, land rights and buildings, including buildings on third-party land, represented EUR 0.7 million of hidden net reserves, with other long-term investments accounting for EUR 3.2 million. Hidden net reserves included hidden liabilities of EUR 0.01 million.

Capital structure
SOVAG's equity capital at the balance sheet date amounted to EUR 14,306,847.07.

SOVAG's equity ratio was 75.0% (2016: 54.8%) in relation to earned premiums for own account. The equity ratio as a percentage of the balance sheet total amounted to 14.0% (2016: 11.4%).

In order to ensure continued compliance with the regulatory solvency capital requirement under Solvency II, in February 2017 the shareholders paid in an additional contribution to capital reserves in the amount of EUR 10.0 million. This capital increase significantly strengthened the coverage ratio (defined as the ratio of eligible capital to solvency capital requirement).

Actuarial reserves
Gross actuarial reserves as at 31 December 2017 amounted to EUR 126.8 million, representing a drop of EUR 54.6 million, or 30.1% year-on-year. After deduction of the reinsurers' share, the remaining net actuarial reserves amounted to EUR 65.8 million (2016: EUR 89.4 million). Relating to earned premiums for own account, this corresponded to a ratio of 344.6% (2016: 318.1%).

The largest proportion of total net actuarial reserves, with EUR 47.9 million, was attributable to the outstanding claims reserve (2016: EUR 65.6 million). The proportion held in foreign currencies was 6.0% at the balance sheet date (2016: 12.1%).

The equalisation reserve and similar provisions stood at EUR 15.9 million at the balance sheet date (2016: EUR 17.3 million).

OUTLOOK

Expectations regarding macroeconomic development

World trade saw robust growth in the financial year 2017 and is increasingly developing in the direction of a globally synchronised upswing. Monetary policy is tending to remain expansionary, with inflation kept low in many places. Opportunities and risks for future economic development appear broadly balanced. In their projections for 2018, the leading economic research institutes are therefore again forecasting above-average world economic growth. With an estimated growth rate of around 3.9%, it is expected to be 0.2 percentage points higher than in 2017.

Expectations on the capital markets

The combination of higher growth, lower inflation and relaxed monetary policy should ensure that high-risk assets such as stocks or higher-yield corporate bonds continue to deliver a positive earnings trend in 2018. However, the high valuation level achieved increases the risk that the global stock exchanges may temporarily perform corrections.

Expectations in Germany's insurance market

The robust upswing in principle also raises demand for insurance products. In the property and accident insurance line of business, the insurance association projected premium growth in the region of 3.0% for 2017. The interest rate environment and the incessant regulatory reforms continue to pose the main challenges. In the medium term, digitalisation opens up opportunities for business activities.

Earnings expectation of the company

The 2018 financial year will continue to be strongly characterised by the restructuring. Following the reduction of the number of contract coverages in direct insurance business from 274,062 to 138,281 in the reporting period, the number of contract coverages was further reduced by 70,163 to 68,118 up to the end of February 2018.

The closing of the portfolio transfer is expected in Q2 2018. With the closing, SOVAG's entire insurance portfolio will be transferred to a new risk carrier, which thus supersedes SOVAG in the role of insurer. The purchase price is EUR 1. When calculating the equalisation payments in respect of outstanding claims for policyholders, 30 June 2017 is taken as a reference date. The adjustment takes account of premiums received and claims payments as well as the run-off of reinsurance contracts. The portfolio transfer will impact on earnings in the financial year in which the transfer is closed.

In the course of the new financial year, work on implementing a new strategy will continue apace. The repositioning is expected to be completed by Q4. However, the company does not anticipate any resulting earnings before 2019.

For 2018 the Management Board predicts a positive result due to the release of the equalisation reserve. It is expected to reach a small single-digit million amount.

RISK REPORT

As part of the implementation of the Solvency II Directive, SOVAG has established the four required governance functions:

- Independent Risk Management function (IRMF, uRCF in German law)
- Compliance function (CF)
- Internal Audit function (IA)
- Actuarial function (AF)

All four governance functions apply the elements of the risk management process described in the following, depending on the respective objective.

RISK MANAGEMENT SYSTEM

In order to adequately measure and manage risks, it is necessary to identify them completely and comprehensively on an ongoing basis. Identified risks are proactively reported to Risk Management by risk officers. Risk Management systematically and comprehensively analyses these risks, and together with the risk officers carries out an assessment of their significance. Risks classified as “significant” are then listed in the risk catalogue. Ongoing monitoring of the risks is the responsibility of Risk Management, while the individual risk officers are in charge of their management. Risk Management also continuously analyses and monitors the effectiveness of the risk actions taken. SOVAG’s current risk situation is regularly discussed and assessed by Risk Management in consultation with the risk officers. Resulting facts and findings that are of relevance for managing risks are reported to the Management Board and the Supervisory Board in regular risk reports.

The risk catalogue is regularly revised and re-evaluated by the risk officers based on the provisions of the risk management guidelines. Additionally, risks are classified based on their assignment in the standard Solvency II tree model. Risks that fall outside of the standard tree model are quantified in an expert evaluation by the risk officers – before and after implementing risk-mitigating measures. Risks that fall outside of the quantification approach are individually assessed for quality after taking the effect of risk-mitigating measures into account.

Internal Audit as a superior body independent of risk processes regularly reviews the efficiency and effectiveness of the risk management system. SOVAG has outsourced this function to an external service provider. In order for Internal Audit to carry out its duties, complete and unrestricted information and audit rights have been granted. As part of multi-year planning, all significant activities, processes, IT systems and the risk management framework are checked for compliance with the risk strategy requirements and to make sure the risk management process is functioning. The Management Board and the Supervisory Board's Audit Committee receive written reports on the results of the audits performed. The audit reports include an evaluation of the audit results as well as suggested actions for eliminating any observed deficiencies and a binding schedule for the concrete implementation of those actions.

Significant risks
SOVAG defines as significant such risks that could have a sustained negative impact on SOVAG's net assets, financial position and results of operations and consequently pose a threat to the company's continued existence as a going concern, its solvability or its rating.

Specifically, SOVAG distinguishes between the following risk categories:

- Underwriting risks
- Investment risks (market risks)
- Currency risks
- Liquidity risks
- Default risk
- Concentration risks
- Operational risks
- Other material risks (strategic risks, legal risks, reputational risks)

Underwriting risks
The variance of the technical result is generally reduced as a result of the broad spread across different lines of business and the capping of exposed risks by means of facultative reinsurance.

The underwriting risk has been significantly reduced as a result of the discontinuation of new underwriting business in 2017. With the transfer of the remaining contract and claims portfolio in 2018, this risk will be eliminated completely.

Investment risks
Under Solvency II requirements, investment risks (market risks in the standard model) are quantified and evaluated for risk exposure in accordance with the standard model.

SOVAG counters interest and exchange rate risks, as well as credit risks, by means of an appropriate diversification of the investments held in the investment portfolio. Further, the credit risk associated with the investments is mitigated by means of regular monitoring and review of the issuers' credit rating. Derivative financial instruments are used selectively within the scope of the respective applicable statutory and regulatory requirements.

The investment portfolio does not contain any asset-backed securities or similar capital market instruments with increased credit risks.

To reduce the operational risks associated with the investments, investment management has been fully outsourced to Ampega Investment GmbH. This risk management includes monthly reporting and risk reports in respect of SOVAG's entire investment portfolio. Where necessary and meaningful, these reports also describe the development of additional risk-mitigating measures.

Currency risks

Currency risks refer to the possibility that currency fluctuations will negatively affect the value of transactions denominated in foreign currencies or net assets and liabilities that are exposed to foreign currency translation risk. Due to the international orientation of the business model, SOVAG is exposed to currency risks, with a focus on the US dollar and the rouble. In respect of the rouble, SOVAG takes these risks into account by to a large extent applying the principle of congruent coverage. Due to the restrictions on payment transactions denominated in US dollars described under "Liquidity risks", it is not possible to ensure congruent coverage in this currency.

Liquidity risks

Liquidity risk describes the risk of being unable to meet present or future payment obligations punctually or in the full amount.

In order to monitor the liquidity risk, the existing liquidity planning has been further developed. All significant cash flows from underwriting business, investments and general administration are recorded, projected and monitored across a rolling three-month period.

Discontinuation of new underwriting business in 2017 and the planned portfolio transfer increase the significance of the liquidity risk for SOVAG.

SOVAG is not directly affected by sanctions imposed against Russia. The intimation of further sanctions by the US Treasury may, however, lead to uncertainty among business partners and in the extreme case to a disruption of banking transactions. There is a risk that this could also affect the generally very solid reinsurance relationships with Russian insurance companies.

Due to the run-off of all reinsurance contracts in connection with the portfolio transfer, this risk no longer applies until final closing.

Default risks

Default risks arise when debtors cannot fulfil their payment obligations to SOVAG. In addition to the default risks associated with investments mentioned earlier, additional default risks exist in respect of direct underwriting business and assumed reinsurance business vis-à-vis policyholders, brokers and reinsurance companies. SOVAG counters these risks by regularly monitoring its outstanding receivables as well as the credit rating of its debtors. SOVAG makes balance sheet provisions for doubtful or irrecoverable receivables in the form of general and specific bad debt allowances and write-downs.

When selecting reinsurers, SOVAG considers a high credit rating to be an important criterion. By continuously monitoring this in accordance with the regulatory requirements, SOVAG limits default risks that could negatively impact its liquidity. Regarding this, SOVAG currently does not see any acute risks.

Closely related to the default risk is the credit risk resulting from a potential downgrade of counterparty credit ratings. Even without there being an actual default, a downgrade would lead to a higher regulatory capital requirement. The risk management framework provides for ongoing monitoring of this risk.

Within the scope of the portfolio transfer, it is planned to terminate all significant reinsurance relationships and to receive corresponding equalisation payments in respect of existing claims. This would eliminate the majority of the existing default risk.

Concentration risks

Concentration risk refers generally to the risk of losses due to a badly diversified investment portfolio; for SOVAG concentration risks may arise as a result of lacking diversification of the investments between different issuers/issuer groups or a high concentration on individual reinsurance partners and brokers.

Since the shareholder SOGAZ provides protection for a large proportion of the active reinsurance business as well as fronting activities, there is a considerable concentration risk in this respect, which is borne by SOVAG. After closing of the portfolio transfer, this risk concentration will cease to exist.

SOVAG's remaining reinsurance programme demonstrates an appropriate diversification over a number of stable reinsurance companies.

At present there are no significant dependencies on individual brokers.

The company has specifically defined the principle of diversification in its internal investment guidelines by setting concentration limits per issuer and line of business. In its monthly risk reports, the asset management company engaged by SOVAG regularly reports on compliance with these requirements at mandate and issuer level. This allows regular and timely monitoring of compliance with the adopted guidelines. At the moment there are no tendencies towards concentration.

Operational risks

Significant operational risks are those that arise as a result of human error, company IT system failure or defects, or as a result of force majeure. Due to the significant reliance of business processes on IT systems, SOVAG is exposed to a variety of operational risks, such as operational failures and business interruptions, data loss as well as external attacks on SOVAG systems. SOVAG counters these risks through extensive protective measures, emergency planning, backup solutions, access controls and other measures. For the purposes of mitigating risks associated with human error, SOVAG has established a broadly based internal control system. This system includes the principle of dual control and automated quality and plausibility controls. Risks arising from force majeure are covered by emergency plans and natural hazard insurance, which are reviewed annually and adjusted as needed.

Other risks

Other risks to which SOVAG is exposed include reputational risk, legal risks and strategic risks.

The company mitigates strategic risks by regularly reviewing the business strategy, controlling strategy implementation and adapting decisions in its core areas of activity to account for changed conditions in the political and economic environment on national and international level. Appropriate staffing and IT resources and equipment to support the corporate strategy are further measures aimed at reducing the strategic risks.

Statutory and regulatory requirements and changes can have a significant influence on SOVAG. The company regularly observes current legislation and jurisdiction on national and international level, enabling it to manage legal risks – including risks under civil law, commercial law, and solvency law as well as under accounting and tax law.

Reputational risks can arise for the company as a result of negative perception by different stakeholder groups – clients, business partners, staff, shareholders, authorities. As a general rule, reputational risks are relevant for companies with a presence in the press. Significant transactions with the potential to cause sustained damage to the reputation of the company must be submitted to the Management Board for a decision. The situation that has arisen due to the discontinuation of active underwriting business is being monitored very closely by the Management Board.

SOLVENCY REQUIREMENTS

The company's own-risk and solvency assessment conducted for 2016 revealed that the current measures are not adequate to guarantee coverage of the solvability capital requirement in 2017. In February 2017, the shareholders injected capital of EUR 10 million into the company to strengthen the solvency situation.

Due to a rating event with the largest reinsurer, the company was temporarily underfunded. The reinsurer's investment grade rating was re-established, enabling the solvency capital requirement to be met again.

OVERALL RISK SITUATION

SOVAG assesses its overall risk position by considering the individual risks and the correlations between these risks and diversification effects as part of its own-risk and solvency assessment (ORSA). SOVAG gains its knowledge of the interdependencies between these risks from observing market data and statistics, as well as from analysis reports from GDV, EIOPA and other trusted sources, plus assessments and analyses of the company's internal data.

Great emphasis is placed on implementation of the portfolio transfer agreement and the foregoing run-off of the reinsurance relationships.

RELATIONS WITH AFFILIATED COMPANIES

SOVAG is affiliated with the following company:

- GAZPROM Germania GmbH, Berlin

SOVAG has prepared a report on relations with affiliated companies pursuant to Section 312 of the German Stock Corporation Act (AktG), which concludes with the following declaration by the Management Board:

"We declare that the company has received appropriate compensation for all transactions and activities listed in the report on relations with affiliated companies, according to the circumstances which were known to us on the date at which said transactions were performed. No action has been taken or omitted on the initiative or in the interest of the companies to be reported on."

Appendix to the management report

INSURANCE LINES AND CLASSES

Health insurance

Other forms of individual non-mandatory insurance

- Travel health insurance

General accident insurance

Individual accident insurance without premium refund

- Travel accident insurance

Group accident insurance without premium refund

- Comprehensive group accident insurance

Liability insurance

Personal liability insurance
(including sports boat and dog-handling liability insurance)

Business and professional liability insurance

- Industrial and commercial operations
- Construction
- Other business and professional liability insurance

Environmental liability insurance

- Water damage liability insurance

Radiation and nuclear installation liability insurance

- Nuclear installation liability insurance

Transport liability insurance

- Traffic liability insurance
- Sea, lake and river transport liability insurance

Other liability insurance not listed

- Home and landowner liability insurance

Motor insurance

Third-party motor insurance
Fully comprehensive motor insurance
Partially comprehensive motor insurance
Motor accident insurance
Other motor insurance not listed

Fire insurance

Industrial fire insurance
Other fire insurance

Burglary, theft and robbery insurance

Mains water damage insurance

Glass insurance

Storm insurance

Comprehensive contents insurance

Comprehensive homeowner's insurance

Engineering insurance
Machinery insurance (including construction machinery insurance)
Electronics insurance
Assembly insurance
Construction insurance
Other engineering insurance not listed

Aviation insurance
Liability insurance
Hull insurance
Aviation accident insurance

Transport insurance
Hull insurance
- Marine hull insurance
- Inland waterway and river navigation hull insurance
- Railway rolling stock fully comprehensive insurance
- Sports boat hull insurance
- Construction risk insurance
- Other fully comprehensive insurance

Cargo insurance
- Cargo insurance
- Fully comprehensive container insurance
- Travel storage insurance
- Other goods insurance
- Securities insurance (commercial)
- War risk insurance
- Other transport insurance not listed
(including insurance for offshore risks)

Credit and guarantee insurance
Other credit and guarantee Insurance not listed
(only for acquired insurance business)

Extended coverage insurance

Business interruption insurance
- Insurance for business interruptions caused by fire
- Technical business interruption insurance
- Other business interruption insurance

Travel assistance insurance

Other indemnity insurance
Other insurance for property damage
- Exhibition insurance
- Chilled cargo insurance
- Property insurance for nuclear installations
- Luggage insurance
- Vehicle luggage insurance
- Insurance for works of art
- Other property insurance not listed

Other insurance for financial loss
- Boycott and strike insurance
- Travel cancellation insurance
- Equipment guarantee insurance
- Loss of rent insurance

Other indemnity insurance not listed

Annual financial statements

BALANCE SHEET
as of 31 December 2017

ASSETS

				31.12.2017	31.12.2016
A. Intangible assets					
I. Internally generated industrial property rights and similar rights and assets			82,819.51		263,381.92
II. Purchased concessions, industrial and similar rights and assets, and licences in such rights and assets			1,579,237.95		2,840,214.39
III. Prepayments			0.00		9,806.20
				1,662,057.46	3,113,402.51
B. Investments					
I. Land, land rights and buildings, including buildings on third-party land			390,626.66		407,002.09
II. Investments in affiliated companies and participations					
1. Participations			0.00		303,168.03
III. Other investments					
1. Shares, investment fund shares/units and other non-fixed-interest securities		33,296,460.03			33,788,523.21
2. Bearer bonds and other fixed-interest securities		30,265,080.14			46,847,079.84
3. Other loans					
a) Registered bonds	2,200,000.00				2,200,000.00
b) Loans and promissory notes	7,498,493.71				11,497,743.27
c) Miscellaneous other loans	211,745.08				1,383,366.57
		9,910,238.79			15,081,109.84
4. Deposits with banks		88,324.73			100,349.54
5. Other investment assets		303,168.03			0.00
			73,863,271.72		95,817,062.43
IV. Deposit with ceding insurers from inward reinsurance business			867,819.92		2,352,334.99
				75,121,718.30	98,879,567.54
C. Receivables					
I. Receivables from direct insurance business due from:					
1. Policyholders of which from affiliated companies EUR 0.00 (2016: EUR 0.00)		335,435.74			867,812.04
2. Brokers		2,017,910.60			3,017,102.82
			2,353,346.34		3,884,914.86
II. Accounts receivable from reinsurance business of which from affiliated companies EUR 0.00 (2016: EUR 0.00)			14,603,070.01		18,382,306.74
III. Other receivables			2,164,709.71		2,716,320.73
				19,121,126.06	24,983,542.33
D. Other assets					
I. Tangible assets and inventories			452,611.14		598,644.71
II. Current bank balances, cheques and cash in hand			5,288,113.79		6,581,117.05
				5,740,724.93	7,179,761.76
E. Prepaid expenses					
I. Deferred interest and rent			333,007.49		659,250.06
II. Other deferred items			130,772.90		117,913.10
				463,780.39	777,163.16
Total assets				**102,109,407.14**	**134,933,437.30**

EQUITY AND LIABILITIES

				31.12.2017	31.12.2016
A. Shareholders' equity					
I. Subscribed capital			9,984,000.00		9,984,000.00
II. Capital reserves			29,369,633.72		19,369,633.72
III. Revenue reserves					
1. Legal reserve		963,086.31			963,086.31
			963,086.31		963,086.31
IV. Net accumulated loss			–26,009,872.96		–14,902,724.86
				14,306,847.07	15,413,995.17
B. Actuarial reserves					
I. Unearned premium reserve					
1. Gross amount		2,889,856.24			10,207,093.39
2. less: reinsurers' share		1,501,204.59			5,572,631.39
			1,388,651.65		4,634,462.00
II. Outstanding claims reserve					
1. Gross amount		107,139,958.95			151,532,475.78
2. less: reinsurers' share		59,256,717.69			85,951,543.44
			47,883,241.26		65,580,932.34
III. Equalisation reserve and similar provisions			15,894,768.00		17,299,469.00
IV. Other actuarial reserves					
1. Gross amount		873,260.89			2,387,554.17
2. less: reinsurers' share		273,148.43			497,035.28
			600,112.46		1,890,518.89
				65,766,773.37	89,405,382.23
C. Other provisions					
I. Provision for pensions and similar obligations			8,852,669.00		8,710,570.00
II. Miscellaneous other provisions			7,090,610.19		4,537,756.94
				15,943,279.19	13,248,326.94
D. Deposits retained from ceding insurers for outward reinsurance business				2,389,670.57	4,205,333.86
E. Other liabilities					
I. Liabilities arising from direct insurance business due to					
1. Policyholders of which to affiliated companies EUR 0.00 (2016: EUR 0.00)		123,122.77			349,708.00
2. Brokers		1,787,336.64			8,114,184.81
			1,910,459.41		8,463,892.81
II. Accounts payable from reinsurance business of which to affiliated companies EUR 0.00 (2016: EUR 2,942,675.90)			422,246.54		3,035,050.56
III. Other liabilities of which to affiliated companies EUR 533,661.45 (2016: EUR 23,800.00) of which taxes: EUR 218,853.63 (2016: EUR 329,921.06) of which social security: EUR 11,093.6 (2016: EUR 12,296.98)			1,370,130.99		1,161,455.73
				3,702,836.94	12,660,399.10
Total equity and liabilities				**102,109,407.14**	**134,933,437.30**

INCOME STATEMENT
for the period from 1 January to 31 December 2017

				2017	2016
I. Technical account					
1. Earned premiums for own account					
a) Gross premiums written		36,015,611.39			52,987,673.22
b) Reinsurance premiums ceded		20,177,409.93	15,838,201.46		26,758,282.90
c) Change in gross unearned premiums		7,317,237.15			2,792,370.30
d) Change in reinsurers' share of unearned premiums		−4,071,426.80	3,245,810.35		−915,799.04
				19,084,011.81	28,105,961.58
2. Other underwriting income for own account				1,646.80	4,103.06
3. Claims expenses incurred for own account					
a) Payments for claims incurred					
aa) Gross amount		78,658,150.76			48,682,208.47
bb) Reinsurers' share		48,822,963.93			20,833,744.91
			29,835,186.83		27,848,463.56
b) Change in outstanding claims reserve					
aa) Gross amount		−42,593,740.38			16,561,192.99
bb) Reinsurers' share		−24,970,415.52			24,053,361.81
			−17,623,324.86		−7,492,168.82
				12,211,861.97	20,356,294.74
4. Change in other actuarial reserves				−1,095,336.01	−1,079,944.61
5. Expenses for profit-related and non-profit-related premium refunds for own account				0.00	−102,362.00
6. Expenses for insurance operations for own account					
a) Gross expenses for insurance operations			13,972,957.42		20,340,101.30
b) less: commissions received and profit-sharing from reinsured business			2,876,640.51		3,135,042.72
				11,096,316.91	17,205,058.58
7. Other underwriting expenses for own account				78,336.01	200,612.65
8. Subtotal				**−3,205,520.27**	**−8,469,594.72**
9. Change in equalisation reserve and similar provisions				−1,404,701.00	3,074,361.00
10. Technical result for own account				**−1,800,819.27**	**−11,543,955.72**

				2017	2016
II. Non-technical account					
1. Investment income					
a) Income from other investments					
of which from affiliated companies EUR 0.00 (2016: EUR 0.00)					
aa) Income from land, land rights and buildings including buildings on third-party land	0.00				2,229.52
bb) Income from other investments	1,325,970.61	1,325,970.61			1,907,871.69
b) Income from reversals		227,311.97			359,441.80
c) Profits from the disposal of investments		616,244.81			2,594,415.76
			2,169,527.39		4,863,958.77
2. Investment expenses					
a) Investment management expenses, interest paid and other investment expenses		528,880.30			711,012.63
b) Write-downs on investments		611,853.36			769,123.06
c) Losses from the disposal of investments		13,233.71			120,576.75
			1,153,967.37		1,600,712.44
				1,015,560.02	3,263,246.33
3. Other income			1,758,895.48		2,187,065.73
4. Other expenses			12,396,690.80		9,098,320.41
				–10,637,795.32	–6,911,254.68
5. Result from ordinary operating activities				**–11,423,054.57**	**–15,191,964.07**
6. Extraordinary income			0.00		0.00
7. Extraordinary expenses			100,965.00		100,965.00
8. Extraordinary result				**–100,965.00**	**–100,965.00**
9. Taxes on income			232,744.58		–185,852.94
10. Other taxes			–649,616.05		–204,351.27
				–416,871.47	**–390,204.21**
11. Net loss for the year				**–11,107,148.10**	**–14,902,724.86**
12. Profit/loss carried forward from previous year				–14,902,724.86	0.00
13. Net accumulated loss				**–26,009,872.96**	**–14,902,724.86**

Notes

The annual financial statements were prepared in accordance with the German Commercial Code [HGB], the German Stock Corporation Act [Aktiengesetz – AktG], the Act on the Supervision of Insurance Undertakings [Versicherungaufsichtgesetz – VAG] and German Accounting Regulations for Insurance Companies [Verordnung über die Rechnungslegung von Versicherungsunternehmen – RechVersV], each in their relevant valid version.

ACCOUNTING AND MEASUREMENT POLICIES

The data processing programs included under **intangible assets** were measured at purchase cost less straight-line amortisation on a pro rata basis. The assets are amortised from their date of completion.

Land and buildings were recognised at cost, less depreciation on buildings. If permanent impairment is likely, land and buildings were carried at cost and – where applicable – adjusted for impairment at the lower of cost or market value pursuant to Section 253 (3) HGB.

Securities classified as current assets were measured at purchase cost or the lower of their fair value or market value pursuant to Section 341b (2), first half-sentence HGB in conjunction with Section 253 (1), sentence 1, and (4) HGB. If the fair value or market value increases, or if there is an improvement in the exchange rate, write-downs are reversed in accordance with Section 253 (5) HGB up to the maximum amount of the relevant purchase cost.

Securities classified as fixed assets were recognised at purchase cost, where applicable less write-downs, to reflect expected permanent impairment necessary for determining the fair value pursuant to Section 341b (2), second half-sentence HGB in conjunction with Section 253 (3) HGB. Permanent impairment occurs with bearer bonds and other fixed-interest securities if the issuer's credit rating deteriorates to a significant extent, namely if the rating is reduced by two or more grades within a financial year or falls below investment grade. Permanent impairment in respect of shares, investment fund shares/units and other non-fixed-interest securities can occur if the fair value over the past six months has persistently remained below 80% of the carrying amount at the measurement date. In the case of pure bond funds, the investment grade rating of the securities held in the bond was monitored for the purpose of assessing impairment. For mixed funds, the securities held in the funds were used for this purpose. Where the reasons for the original write-downs no longer apply, they are reversed in accordance with Section 253 (5) HGB up to the maximum amount of the purchase cost.

Registered bonds were recognised with their nominal value pursuant to Section 341c (1) HGB and are only written down in the case of expected permanent impairment caused by a downgrading of the credit rating. Where the reasons for the original write-downs no longer apply, they are reversed in accordance with Section 253 (5) HGB up to the maximum amount of the purchase cost.

Loans and promissory notes were measured at purchase cost or at their lower fair value if this results from exchange rate fluctuations or expected permanent impairment of value due to deterioration of the credit rating. Where the reasons for the original write-downs no longer apply, they are reversed in accordance with Section 253 (5) HGB up to the maximum amount of the purchase cost.

Miscellaneous other loans were recognised at their purchase cost and only written down in the event of falling exchange rates or expected permanent impairment of value due to a deterioration of the credit rating. In the event of an increase in exchange rates, write-downs were reversed in accordance with Section 253 (5) HGB up to the maximum amount of the purchase cost.

Deposits with banks denominated in foreign currencies were valued at the reference rate of the European Central Bank (ECB) at year end. Deposits in euros were posted at their nominal amount.

Other investments were measured at purchase cost or, in the case of expected permanent impairment, at their lower fair value in accordance with Section 253 (3) HGB.

Deposits with ceding insurers from inward reinsurance business were stated at their nominal value.

Receivables from **direct insurance business** and **accounts receivable from reinsurance business** were carried at their nominal value less write-downs of receivables. The write-downs of receivables also take account of existing risks that might occur in connection with the continuous adjustment of current accounts (receivables and payables from direct insurance business).

In the case of **other receivables** and **other assets**, measurement was based on purchase cost or nominal value. Tangible assets are recognised at their purchase cost less straight-line depreciation, taking account of the expected useful life. Low-value assets with a net value of up to EUR 150.00 were fully written down in the year of acquisition. Low-value assets with a purchase cost of between EUR 150.00 and EUR 1,000.00 were carried in a collective item under assets and written down over a five-year period irrespective of whether they continue to be recognised as assets and regardless of when they were acquired within the financial year. Depreciation on all additions to tangible assets with an acquisition value of more than EUR 1,000.00 was recognised on a pro rata basis. In the year of acquisition, these assets were written down only on a pro rata basis for the full month of acquisition and the subsequent months.

Current bank balances, cheques and cash in hand were assessed at their nominal value.

Prepaid expenses consist of accrued interest from the last due date up to the balance sheet date and expenses allocatable to the subsequent accounting period on a proportional straight-line basis.

Unearned premiums for direct insurance business were as a general rule calculated pro rata temporis. The specifications from the Coordinated Decree of the Tax Authorities of the Federal States (koordinierter Ländererlass) dated 30 April 1974 have been taken into account. In respect of direct transport business, the unearned premium reserve was taken into account when calculating the outstanding claims reserve.

In **inward reinsurance business**, unearned premiums were in principle calculated on the basis of data provided by the ceding insurers. In the third-party motor insurance segment, the unearned premium reserve for border policies in inward reinsurance business was calculated for mandatory contracts based on the 1/8 method. In respect of mandatory contracts from the London branch in the property, technical and transport business lines, the 1/24 method was used. The shares of reinsurers in the unearned premium reserve both in direct and indirect insurance business were calculated using the same method.

The **outstanding claims reserve in the company's direct insurance business** was recognised in equity based on the anticipated expense for each individual claim. Receivables from recoveries, salvages and partial agreements were deducted from the provisions. For as yet unknown loss events, provisions for losses incurred but not reported (IBNR) have been taken into account, calculated using actuarial methods. The internal provisions for claims settlement expenses were determined on a lump-sum basis, taking into account the ratio of paid claims settlement expenses to payments for claims and total outstanding claims reserve.

In direct transport insurance business, the forming of provisions was fundamentally based on the principle of individual valuation. In cases where no individual provision could be formed, the zero position system was used for the financial year. For older underwriting years, a flat-rate calculation was made based on empirical values assuming a fall in percentage rates. Within three years at the latest, provisions for all losses will be formed in accordance with general principles.

In **inward reinsurance business**, pro rata provisions were generally formed at the request of the initial insurer; in all other cases using estimates based on payments for claims made in previous years for known loss events, plus allowances for unknown events that have been incurred but not reported (IBNR).

The **shares of reinsurers** in the outstanding claims reserve, including claims settlement costs, were calculated based on contractual agreements.

The **equalisation reserve** pursuant to Section 341h HGB in conjunction with Section 29 RechVersV and the nuclear installation provision were formed based on the legal reserve and the instructions of the Federal Financial Supervisory Authority (BaFin).

The **cancellation provision** was recognised for elimination or reduction of the underwriting risk in an amount corresponding to the likely future default. The proportion of this provision relating to outward reinsurance business corresponds to the reinsurer's share in the risk.

The provision for **obligations from membership of the association for victims of traffic accidents** [Verein Verkehrsopferhilfe e.V.] was recognised based on the instructions of this association. It corresponds to the proportion set out in our articles of association.

The basis for measuring the **provision for contingent liabilities** was the expected premium, claims and cost development in the relevant line of business. The remaining actuarial reserves were calculated based on the expected requirement.

Contractual obligations to reinstate reinsurance premiums were taken into account by creating a corresponding **provision for reinstatement premiums**.

Provisions for pensions were calculated in accordance with recognised actuarial principles using the projected unit credit method (PUC method). The amount of this provision, based on the PUC method, is defined as the actuarial present value of pension entitlements (or "defined benefit obligation") accrued at the balance sheet date by employees in accordance with pension formulas and vesting practices based on their past service to the company. The amount of the provision is calculated taking account of trend assumptions regarding future developments relating to entitlements and pensions, plus any likely fluctuations. The 2005 G reference tables drawn up by Professor Klaus Heubeck were used as a biometric calculation basis. The following additional assumptions underpin the assessment: average interest rate of 3.68% (2016: 4.01%) based on the past ten years and an average interest rate of 2.80% (2016: 3.24%) based on the past seven years, assuming a remaining life of 15 years respectively; salary trend remains unchanged at 2.50% p.a., assessment ceiling trend remains unchanged at 2.00% p.a. and retirement trend at 1.75% p.a. (2016: 2.00%).

Calculating the difference amount in accordance with Section 253 (6) HGB	**in EUR thousands**
Provision recognised in the balance sheet using the ten-year average interest rate	8,853
Provision using the seven-year average interest rate	10,148
Difference in accordance with Section 253 (6) HGB	1,295

The 1/15 rule was applied when reporting provision for pensions. The difference in the pension obligation as at 1 January 2010 was accounted for at the minimum amount (1/15 of EUR 1.5 million). The remaining difference is reported over the following years. In the financial year 2017, the minimum amount of EUR 0.1 million was reversed. The remaining difference in the amount of EUR 0.7 million corresponds to 7/15. Expenses from the first-time application of the German Accounting Law Modernisation Act (BilMoG) from 1 January 2010 are shown in the extraordinary result in accordance with Section 67 (1), sentence 1 of the Introductory Act to the German Commercial Code (EGHGB).

The **provision for anniversaries** was calculated in accordance with recognised actuarial principles using the PUC method. The amount of this provision, based on the PUC method, is defined as the actuarial present value of the anniversary bonuses accrued pro rata as at the balance sheet date. The amount of this provision is calculated taking account of trend assumptions regarding future developments relating to entitlements and pensions, plus any likely fluctuations. The 2005 G reference tables drawn up by Professor Klaus Heubeck were used as a biometric calculation basis. The following additional assumptions underpin the assessment: underlying interest rate of 2.8% p.a. (2016: 3.24%) assuming a remaining life of 15 years; salary trend remains unchanged at 2.25% p.a. and assessment ceiling trend remains unchanged at 2.00% p.a. The amount permissible under commercial law was recognised.

Other non-actuarial reserves are recognised in an amount deemed appropriate to meet the obligations based on prudent business judgement. Where other non-actuarial reserves related to a period of more than one year, the reserves were discounted in accordance with Section 253 (2) HGB on the basis of the discount rates published by Deutsche Bundesbank.

Deposits retained from ceding insurers for outward reinsurance business and liabilities from direct insurance business plus **accounts payable from reinsurance business** and **other liabilities** are recognised at the settlement amount.

NOTES TO THE BALANCE SHEET

ASSETS

Development of asset items A., B. I. to III. in the financial year 2017	Carrying amounts 2016 in EUR	Additions in EUR	Reclassifications in EUR
A. Intangible assets			
1. Internally generated industrial property rights and similar rights and assets	263,381.92	17,870.82	
2. Purchased concessions, industrial and similar rights and assets, and licences in such rights and assets	2,840,214.39	11,675.69	
3. Prepayments	9,806.20		
Total A.	**3,113,402.51**	**29,546.51**	**0.00**
B. I. Land, land rights and buildings, including buildings on third-party land	407,002.09		
B. II. Investments in affiliated companies and participations			
1. Participations	303,168.03		–303,168.03
Total B. II.	**303,168.03**	**0.00**	**–303,168.03**
B. III. Other investments			
1. Shares, investment fund shares/units and other non-fixed-interest securities	33,788,523.21	63,360.00	0.00
2. Bearer bonds and other fixed-interest securities	46,847,079.84	0.00	0.00
3. Other loans			
a) Registered bonds	2,200,000.00	0.00	0.00
b) Loans and promissory notes	11,497,743.27	750.44	0.00
c) Miscellaneous other loans	1,383,366.57	2,454.20	0.00
4. Deposits with banks	100,349.54	0.00	0.00
5. Other investment assets	0.00	0.00	303,168.03
Total B. III.	**95,817,062.43**	**66,564.64**	**303,168.03**
Total B. I. to B. III.	**96,527,232.55**	**66,564.64**	**0.00**
Total	**99,640,635.06**	**96,111.15**	**0.00**

	Disposals in EUR	Reversals in EUR	Write-downs in EUR	Exchange rate gains (+)/ losses (–) in EUR	Carrying amounts 2017 in EUR	in %	Fair values 2017 in EUR
			198,433.23		82,819.51		
			1,272,652.13		1,579,237.95		
	9,806.20				0.00		
	9,806.20	**0.00**	**1,471,085.36**	**0.00**	**1,662,057.46**		**1,662,057.46**
			16,375.43		390,626.66	0.5	1,073,400.00
					0.00	0.0	0.00
	0.00	**0.00**	**0.00**	**0.00**	**0.00**	**0.0**	**0.00**
	136,062.14	130,553.06	549,914.10	0.00	33,296,460.03	44.8	34,774,633.10
	16,602,127.69	93,497.35	44,796.74	–28,572.62	30,265,080.14	40.8	31,060,915.85
	0.00	0.00	0.00	0.00	2,200,000.00	3.0	2,436,219.16
	4,000,000.00	0.00	0.00	0.00	7,498,493.71	10.1	8,208,425.25
	1,176,570.16	3,261.56	767.09	0.00	211,745.08	0.3	211,745.08
	12,024.81	0.00	0.00	0.00	88,324.73	0.1	88,324.73
	0.00	0.00	0.00	0.00	303,168.03	0.4	303,168.03
	21,926,784.80	**227,311.97**	**595,477.93**	**–28,572.62**	**73,863,271.72**	**99.5**	**77,083,431.20**
	21,926,784.80	**227,311.97**	**611,853.36**	**–28,572.62**	**74,253,898.38**	**100.0**	**78,156,831.20**
	21,936,591.00	**227,311.97**	**2,082,938.72**	**–28,572.62**	**75,915,955.84**		**79,818,888.66**

B. Investments

Fair value of investments

Land is valued using the income capitalisation approach. The most recent valuation of the plot of land still existing as at the balance sheet date was made in Q1 2017. For bearer bonds and shares, the fair value of securities traded on the stock exchange was based on the stock market prices as at the balance sheet date. Investment fund shares were recognised at their redemption prices. For other loans for which no market prices were available, fair value was determined on the basis of yield curves.

As at the balance sheet date, shares, investment fund shares/units and other non-fixed-interest securities are allocated to fixed assets with a carrying amount totalling EUR 28,990 thousand (2016: EUR 30,337 thousand). Write-downs of EUR 12 thousand (2016: EUR 0 thousand) were thus avoided. For securities measured in accordance with Section 341b (2), second half-sentence HGB in conjunction with Section 253 (3) HGB, write-downs of EUR 259 thousand were recognised to reflect expected permanent impairment.

Based on the prices as at the balance sheet date, the hidden reserves and liabilities attributable to these securities developed as follows:

Investment class in EUR thousands	Hidden reserves 2017	Hidden liabilities 2017	Hidden net reserves (+)/ liabilities (–) 2017	Hidden net reserves (+)/ liabilities (–) 2016
Investment fund shares	306	–12	294	173
Total	**306**	**–12**	**294**	**173**

It can be assumed that the hidden liabilities attributable to the securities measured in accordance with Section 341b (2), second half-sentence HGB in conjunction with Section 253 (3) HGB do not reflect permanent impairments.

B. III.1. Investment funds with a shareholding of more than 10%

SOVAG has established a special investment fund, the SSF Fund, in which it holds 100% of the shares. The SSF Fund is a mixed securities fund, in which up to 20% of the fund volume may be invested in shares, investment fund shares/units and other non-fixed-interest securities. At year end, the SSF Fund was recognised with a carrying amount of EUR 27,587 thousand (2016: EUR 27,501 thousand). In the financial year 2017, EUR 86 thousand was recognised for reversals of prior-period impairment losses. The market value as at the balance sheet date was EUR 27,675 thousand, whereby EUR 88 thousand (2016: EUR 0 thousand) represents hidden reserves. For the financial year 2017, ordinary income of EUR 317 thousand was taken to retained profits (2016: dividend distribution of EUR 398 thousand). The option to return units on a daily basis is not restricted. Since 2011, the special fund has been classified under fixed assets.

B. III.2. and B. III.3a/b) Bond structures

The following simply structured products in accordance with BaFin circular R 3/99 were held in the portfolio as at 31 December 2017:

Bond structuring in EUR thousands	Carrying amount 2017	Market value 2017	Carrying amount 2016	Market value 2016
Callable bonds	1,873	2,127	3,873	4,569
of which:				
Bearer bonds	373	419	373	473
Registered bonds	1,000	1,130	1,000	1,038
Promissory notes	500	578	2,500	3,058
Floating rate notes	**3,000**	**3,183**	**3,000**	**3,159**
of which:				
Bearer bonds	0	0	0	0
Promissory notes	3,000	3,183	3,000	3,159
Total	**4,873**	**5,310**	**6,873**	**7,728**
Share in the investment portfolio excl. deposits with ceding insurers in %	6.6	6.8	7.1	7.6

As at 31 December 2017 the portfolio contained no derivative financial assets.

B. III.3c) Miscellaneous other loans

Miscellaneous other loans relate with EUR 95 thousand to a loan granted to an employee as well as miscellaneous other loans amounting to EUR 117 thousand.

D. Other assets

In connection with sanctions against Russia, correspondent banks have frozen current incoming and outgoing payments in USD and GBP to the value of EUR 75 thousand. SOVAG will apply for their release to the Office of Foreign Assets Control (OFAC) in due course.

EQUITY AND LIABILITIES

A. Shareholders' equity

A. I. Subscribed capital

The share capital is divided into 19,500 registered shares with a par value of EUR 512.00 each. GAZPROM Germania GmbH (GPG), Berlin, holds 50.1% of these shares, INSURANCE COMPANY OF GAZ INDUSTRY SOGAZ (SOGAZ), Moscow, holds 25.1% and VOLGA Resources Investments S.A. (VOLGA), Luxembourg, holds 24.8%.

A. II. Capital reserves

Capital reserves were formed in accordance with Section 272 (2) No. 4 HGB. In the financial year 2017 EUR 10,000 thousand was paid into capital reserves.

A. III. Revenue reserves

In accordance with Section 268 (8) HGB, internally generated intangible fixed assets in the amount of EUR 83 thousand (2016: EUR 263 thousand) are subject to a payout block.

Changes in equity in EUR thousands	**2017**	**2016**
I. Subscribed capital	9,984	9,984
II. Capital reserves		
Balance at 1 January	19,370	4,577
Appropriation to capital reserves	10,000	14,793
Withdrawal from capital reserves	0	0
Balance at 31 December	29,370	19,370
III. Revenue reserves		
1. Legal reserve		
Balance at 1 January	963	963
Appropriation to legal reserve	0	0
Balance at 31 December	963	963
IV. Net accumulated loss	–26,010	–14,903
Total	**14,307**	**15,414**

The net accumulated loss of SOVAG is as follows:

Changes in net accumulated loss in EUR thousands	**2017**	**2016**
Net loss for the financial year	–11,107	–14,903
Profit/loss carried forward from previous year	–14,903	0
Subtotal	–26,010	–14,903
Withdrawal from capital reserves	0	0
Net accumulated loss	**–26,010**	**–14,903**

B. Actuarial reserves

The allocation of gross actuarial reserves to the individual insurance classes, groups of classes and segments is as follows:

Gross actuarial reserves in EUR thousands	2017	2016
Direct underwriting business		
Liability insurance	8,734	9,557
Third-party motor insurance	40,311	52,515
Other motor insurance	1,999	2,430
Fire and property insurance	18,772	30,266
comprising:		
Fire insurance	8,069	9,582
Comprehensive homeowner's insurance	4,181	6,699
Other property insurance	6,521	13,985
Transport insurance	20,243	19,871
Other insurance classes	15,394	12,882
Total	**105,454**	**127,520**
Inward reinsurance business	**21,344**	**53,907**
Total underwriting business	**126,798**	**181,427**

B. I. Unearned premium reserve

Gross unearned premiums in EUR thousands	2017	2016
Direct underwriting business		
Liability insurance	204	504
Third-party motor insurance	989	2,252
Other motor insurance	265	507
Fire and property insurance	265	1,634
comprising:		
Fire insurance	69	374
Comprehensive homeowner's insurance	69	461
Other property insurance	127	798
Transport insurance	0	0
Other insurance classes	672	1,235
Total	**2,396**	**6,131**
Inward reinsurance business	**494**	**4,076**
Total underwriting business	**2,890**	**10,207**

B. II. Outstanding claims reserve

Gross outstanding claims reserve in EUR thousands	2017	2016
Direct underwriting business		
Liability insurance	6,329	7,271
Third-party motor insurance	34,623	45,049
Other motor insurance	750	1,157
Fire and property insurance	16,071	23,358
comprising:		
Fire insurance	5,679	6,677
Comprehensive homeowner's insurance	4,109	5,866
Other property insurance	6,284	10,815
Transport insurance	15,081	18,039
Other insurance classes	14,306	10,282
Total	**87,160**	**105,156**
Inward reinsurance business	**19,980**	**46,377**
Total underwriting business	**107,140**	**151,532**

B. III. Equalisation reserve and similar provisions

Equalisation reserve and similar provisions in EUR thousands	2017	2016
Direct underwriting business		
Liability insurance	2,168	1,671
Third-party motor insurance	4,639	5,015
Other motor insurance	976	644
Fire and property insurance	2,299	4,536
comprising:		
Fire insurance	2,233	2,428
Comprehensive homeowner's insurance	0	0
Other property insurance	65	2,108
Transport insurance	4,916	1,523
Other insurance classes	28	457
Total	**15,024**	**13,845**
Inward reinsurance business	**870**	**3,454**
Total underwriting business	**15,895**	**17,299**

Allocatable to equalisation reserve:

Equalisation reserve in EUR thousands	2017	2016
Direct underwriting business		
Liability insurance	2,168	1,671
Third-party motor insurance	4,639	5,015
Other motor insurance	976	644
Fire and property insurance	2,299	4,536
comprising:		
Fire insurance	2,233	2,428
Comprehensive homeowner’s insurance	0	0
Other property insurance	65	2,108
Transport insurance	4,916	1,523
Other insurance classes	28	456
Total	**15,024**	**13,845**
Inward reinsurance business	**870**	**2,187**
Total underwriting business	**15,895**	**16,032**

Allocatable to similar provisions:

Similar provisions in EUR thousands	2017	2016
Nuclear installation provision in inward reinsurance business	0	1,267

B. IV. Other actuarial reserves

Other gross actuarial reserves in EUR thousands	2017	2016
Direct underwriting business		
Liability insurance	34	111
Third-party motor insurance	61	200
Other motor insurance	8	122
Fire and property insurance	136	737
comprising:		
Fire insurance	88	102
Comprehensive homeowner’s insurance	3	371
Other property insurance	45	264
Transport insurance	246	309
Other insurance classes	388	909
Total underwriting business	**873**	**2,388**

Allocatable to cancellation provision:

Gross cancellation provision in EUR thousands	2017	2016
Direct underwriting business		
Liability insurance	34	51
Third-party motor insurance	13	84
Other motor insurance	8	10
Fire and property insurance	20	75
comprising:		
Fire insurance	1	2
Comprehensive homeowner's insurance	3	19
Other property insurance	17	54
Transport insurance	19	16
Other insurance classes	388	592
Total underwriting business	**482**	**829**

Allocatable to the provision for reinstatement premiums:

Gross provision for reinstatement premiums in EUR thousands	2017	2016
Direct underwriting business		
Other motor insurance	0	11
Fire and property insurance	116	270
comprising:		
Fire insurance	88	101
Other property insurance	28	169
Transport insurance	228	258
Total underwriting business	**343**	**538**

Allocatable to the provision for traffic accident victims:

Gross provision for traffic accident victims in EUR thousands	2017	2016
Direct underwriting business		
Third-party motor insurance	47	52
Total underwriting business	**47**	**52**

The provision for contingent liabilities included in gross actuarial reserves was reversed in the financial year 2017 due to the elimination of the underwriting risks in 2018 (2016: EUR 968 thousand).

C. Other provisions

C. I. Provision for pensions and similar obligations

This item includes provisions for active and former members of the Management Board.

in EUR thousands	2017	2016
Provision for pensions	8,853	8,711

C. II. Miscellaneous other provisions

This item includes provisions for:

Miscellaneous other provisions in EUR thousands	2017	2016
Restructuring costs	2,677	0
Severance payments	2,205	1,289
Variable remuneration components/bonuses/one-off payments	690	692
Costs for year-end financial statements	415	566
Outstanding supplier invoices	321	1,233
Legal disputes	250	47
Outstanding salary obligations	225	341
Commission entitlements	142	151
Document retention costs	39	33
Anniversary expenses	34	90
Holiday entitlements	33	52
Remuneration of the Supervisory Board	24	22
Overtime pay	23	3
Contributions to employers' liability insurance association	13	17
Total	**7,091**	**4,538**

NOTES TO THE INCOME STATEMENT

I. TECHNICAL ACCOUNT

Disclosures in accordance with Section 51 (4) No. 1 a–g RechVersV

	Gross premiums written		Gross premiums earned	
in EUR thousands	**2017**	**2016**	**2017**	**2016**
Direct underwriting business				
Liability insurance	2,063	4,074	2,362	4,286
Third-party motor insurance	7,030	9,307	8,293	9,586
Other motor insurance	1,559	2,084	1,801	1,844
Fire and property insurance	5,908	9,098	7,276	9,621
comprising:				
Fire insurance	1,753	3,260	2,058	3,300
Comprehensive homeowner’s insurance	1,564	7,971	1,956	8,030
Other property insurance	2,590	–2,133	3,261	–1,709
Transport insurance	5,661	5,529	5,661	5,530
Other insurance classes	4,893	6,526	5,455	7,503
Total	**27,113**	**36,617**	**30,849**	**38,369**
Inward reinsurance business	**8,902**	**16,371**	**12,484**	**17,411**
Total underwriting business	**36,016**	**52,988**	**43,333**	**55,780**

	Net premiums earned		Gross claims expenses	
in EUR thousands	**2017**	**2016**	**2017**	**2016**
Direct underwriting business				
Liability insurance	1,979	3,970	1,129	2,441
Third-party motor insurance	3,924	6,492	6,712	6,654
Other motor insurance	911	1,144	947	1,143
Fire and property insurance	2,143	5,721	6,504	19,016
comprising:				
Fire insurance	773	911	2,835	4,819
Comprehensive homeowner’s insurance	301	2,801	2,809	8,065
Other property insurance	1,069	2,010	860	6,132
Transport insurance	4,921	4,264	3,042	2,426
Other insurance classes	2,321	2,668	11,644	5,908
Total	**16,199**	**24,259**	**29,979**	**37,588**
Inward reinsurance business	**2,885**	**3,847**	**6,086**	**27,655**
Total underwriting business	**19,084**	**28,106**	**36,064**	**65,243**

in EUR thousands	Gross expenses for insurance operations 2017	2016	Reinsurance balance (+ = expense, – = income) 2017	2016
Direct underwriting business				
Liability insurance	1,248	1,937	–214	–230
Third-party motor insurance	1,491	2,053	–1,093	1,967
Other motor insurance	339	449	–476	–79
Fire and property insurance	3,798	7,939	–1,178	9,745
comprising:				
Fire insurance	1,236	1,610	909	1,221
Comprehensive homeowner's insurance	877	3,876	–297	–113
Other property insurance	1,685	2,454	–1,789	8,638
Transport insurance	2,215	1,656	2,064	–953
Other insurance classes	1,367	1,755	6,105	–2,132
Total	**10,458**	**15,789**	**5,209**	**8,319**
Inward reinsurance business	**3,515**	**4,551**	**–2,829**	**12,372**
Total underwriting business	**13,973**	**20,340**	**2,380**	**20,691**

in EUR thousands	Technical result for own account (– = expense, + = income) 2017	2016
Direct underwriting business		
Liability insurance	–649	–908
Third-party motor insurance	–488	–1,265
Other motor insurance	–189	–407
Fire and property insurance	–1,719	–5,300
comprising:		
Fire insurance	–1,058	–1,182
Comprehensive homeowner's insurance	–1,691	–3,542
Other property insurance	1,030	–575
Transport insurance	–892	–649
Other insurance classes	–501	–2,347
Total	**–4,438**	**–10,876**
Inward reinsurance business	**2,638**	**–668**
Total underwriting business	**–1,801**	**–11,544**

I. 1. a) Gross premiums written

Gross premiums written in direct insurance business are broken down by origin as follows:

in EUR thousands	2017	2016
Germany	10,219	23,247
Euro zone	16,870	12,825
Third countries	25	545
Total	**27,113**	**36,617**

I. 3. Claims expenses incurred for own account

SOVAG's outstanding claims reserve was adequate in accordance with the German prudence concept. Overall, the run-off of the original provisions from the prior period for outstanding claims for own account produced a profit of EUR 8,019 thousand. In relation to the original provisions for total underwriting business for own account, a run-off profit of EUR 12.23% (2016: 11.66%) resulted.

I. 6. a) Gross expenses for insurance operations

Gross expenses for insurance operations are allocatable to:

in EUR thousands	2017	2016
Acquisition costs	6,677	12,627
Administration expenses	7,295	7,713
Total	**13,973**	**20,340**

II. NON-TECHNICAL ACCOUNT

II. 2. b) Write-downs on investments

In accordance with Section 341b HGB in conjunction with Section 253 (3) HGB, write-downs of investment fund shares classified as fixed assets totalling EUR 432 thousand were recognised in the financial year 2017 to reflect expected permanent impairment.

Write-downs of investments classified as current assets of EUR 162 thousand were recognised in accordance with Section 341b HGB in conjunction with Section 253 (4) HGB. These related with EUR 117 thousand to shares and with EUR 45 thousand to bearer bonds.

II. 3. Other income

Other income primarily relates to income from the reversal of other provisions (EUR 682 thousand) and income arising from exchange rate differences (EUR 358 thousand). Further significant components are service income through the Green Card system under the London Agreement (EUR 151 thousand).

II. 4. Other expenses

Other expenses relate mainly to expenses which affect the company as a whole (EUR 8,571 thousand). This item also principally includes expenses for outstanding bonuses in connection with the transfer of the insurance portfolio (EUR 2,000 thousand), expenses arising from exchange rate differences (EUR 1,097 thousand), interest cost of provisions (EUR 377 thousand) and service cost (EUR 190 thousand).

II. 7. Extraordinary expenses

The transition to the German Accounting Law Modernisation Act (BilMoG) from 1 January 2010, gave rise to a difference of EUR 1.5 million due to the change in the assessment approach of provisions for pensions and similar obligations. This amount is accumulated in accordance with Section 67 (1) of the Introductory Act to the German Commercial Code (EGHGB) with 1/15 per year up to 31 December 2024. The minimum allocation amount is EUR 101 thousand per year. A higher addition than this amount may be made annually. In the 2017 reporting year, EUR 101 thousand was appropriated.

II. 9. Taxes on income

Taxes on income relate principally to tax payments for prior years arising from the tax audit carried out in the reporting year for the years 2012 to 2015. The results have been included in full in the annual financial statements.

II. 10. Other taxes

Other taxes concern prepaid VAT assets from the reporting year as well as tax rebates due to continuous assessments and the tax audit.

OTHER DISCLOSURES

Maturity of liabilities

The liabilities presented in the balance sheet all have maturities of less than 12 months and are not secured by liens or similar rights.

Changes in the portfolio of direct insurance policies written for own account in the financial year 2017 with maturities of at least one year

in units	Number of policies at end of prior period	Number of policies at end of current period	Change	Number of policies as at end of February 2018
Liability insurance	32,685	16,590	–16,095	241
Third-party motor insurance	86,709	50,458	–36,251	32,180
Other motor insurance	29,740	15,240	–14,500	12,533
Fire and property insurance	60,132	24,104	–36,028	5,573
comprising:			0	
Fire insurance	11,500	3,066	–8,434	88
Comprehensive homeowner's insurance	7,857	2,119	–5,738	161
Other property insurance	40,775	18,919	–21,856	5,324
Transport insurance	828	952	124	288
Other insurance classes	63,968	30,937	–33,031	17,303
Total	**274,062**	**138,281**	**–135,781**	**68,118**

Commissions and other remuneration of insurance agents, personnel expenses

in EUR thousands	2017	2016
1. Commissions of all kinds to insurance agents within the meaning of Section 92 HGB for direct insurance business	6,533	10,460
2. Wages and salaries	8,078	7,559
3. Social security and other employee benefit costs	622	806
4. Post-employment benefit costs	35	0
5. Total expenses	**15,268**	**18,825**

Average number of employees

in EUR	2017	2016
Office staff	56	78

SOVAG has no sales force, there is no need for grouping as the company employs exclusively salaried staff.

Management Bodies
The members of the Supervisory Board and the Management Board are listed on pages 6/7 of this Annual Report.

Remuneration of the Management Bodies
The disclosures required by Section 285 Nos. 9a and b HGB regarding the total remuneration of the members of the Management Bodies are omitted pursuant to Section 286 (4) HGB, because the remuneration of a member of these bodies could be identified as a result of these disclosures.

A loan of EUR 50 thousand and a loan of EUR 125 thousand were granted to a retired member of the Management Board within the meaning of Section 285 No. 9c HGB. Both loans fell due in 2017 following termination of the employment contract and were netted/settled with outstanding salary payments.

Remuneration of the Supervisory Board for the 2017 reporting year which, in accordance with the articles of association is to be determined by resolution of the shareholders' meeting, was taken into account with EUR 24 thousand.

Related party disclosures
Transactions with related parties were conducted at prevailing market terms.

Contingent liabilities and other financial commitments
Framework contracts for the provision of IT services were concluded for an indefinite period between SOVAG and two service providers. The first contract with Braunschweig-IT GmbH may be terminated by either party subject to a 12-month period of notice to the end of the calendar year. The IT contract with GAZPROM Germania GmbH may be terminated with a 12-month period of notice to the end of the next calendar month, at the earliest at 31 December 2019. SOVAG's financial commitments up to the first possible termination date are in line with generally accepted market practices. Service and maintenance expenses in the reporting year ran to EUR 1,166 thousand, of which EUR 534 thousand relate to expenses to affiliated companies.

Further, commitments exist in respect of rent and leasing contracts within normal business limits. The rental contract concluded with Deka Immobilien Investment GmbH for the office premises at the company's registered office has a fixed term of ten years, the earliest termination date being to 31 July 2025. Total future payment commitments under rent and leasing contracts amount to EUR 4,043 thousand.

There are no risks within the meaning of Section 285 No. 27 HGB and no other financial obligations in respect of post-employment benefits over and above the provisions for pensions disclosed in the balance sheet.

Auditor's fees

The total auditor's fees for the financial year 2017 amounted to:

in EUR thousands	Total fee 2017
a) Financial statements audit	309
b) Tax advisory services	1
c) Other services	141
	451

Other services principally relate to assurance reviews and analyses in connection with the portfolio transfer and consultancy services in respect of Solvency II requirements.

Deferred taxes

As at 31 December 2017, there was an excess of deferred tax assets over deferred tax liabilities. This asset surplus results mainly from the temporary valuation differences for the outstanding claims reserve arising from the more realistic valuation and discounting required for tax accounting purposes, as well as existing tax loss carryforwards. Deferred tax liabilities, on the other hand, result primarily from the recognition of internally generated intangible fixed assets in the German GAAP financial statements, and different valuation approaches for investments. The total tax rate to be applied is around 30%.

On the basis of the existing recognition option in the case of an excess of deferred tax assets under Section 274 HGB, the company has opted not to recognise deferred taxes.

Events after the reporting date

At the extraordinary shareholders' meeting of 20 February 2018, the shareholders approved the portfolio transfer agreement with a new risk carrier dated 31 December 2017.

Consolidated financial statements

Effective from 23 December 2015, GAZPROM Germania GmbH (GPG), Berlin, holds a majority of 50.1% of the shares in SOVAG, INSURANCE COMPANY OF GAZ INDUSTRY SOGAZ (SOGAZ), Moscow, holds 25.1% of the voting rights (formerly 50.9%). SOVAG is included in the consolidated financial statements of both SOGAZ and GPG using the equity method of accounting in compliance with International Financial Reporting Standards (IFRSs). The consolidated financial statements are available from the registered office of the respective company or via their websites (https://www.sogaz.ru and https://www.gazprom-germania.de).

Hamburg, 27 March 2018

The Management Board

Arndt Gossmann　　　　Dr Gerd H. Meyer

INDEPENDENT AUDITOR'S REPORT

To Schwarzmeer und Ostsee Versicherungs-Aktiengesellschaft SOVAG, Hamburg

REPORT ON THE AUDIT OF THE ANNUAL FINANCIAL STATEMENTS AND OF THE MANAGEMENT REPORT

Audit Opinions

We have audited the annual financial statements of Schwarzmeer und Ostsee Versicherungs-Aktiengesellschaft SOVAG, Hamburg, which comprise the balance sheet as at 31 December 2017, and the statement of profit and loss for the financial year from 1 January 2017 to 31 December 2017, and notes to the financial statements, including the recognition and measurement policies presented therein. In addition, we have audited the management report of Schwarzmeer und Ostsee Versicherungs-Aktiengesellschaft SOVAG for the financial year from 1 January 2017 to 31 December 2017. We have not audited the content of those parts of the management report listed in the "Other Information" section of our auditor's report in accordance with the German legal requirements.

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

- the accompanying annual financial statements comply, in all material respects, with the requirements of German commercial law and give a true and fair view of the assets, liabilities and financial position of the Company as at 31 December 2017 and of its financial performance for the financial year from 1 January 2017 to 31 December 2017 in compliance with German Legally Required Accounting Principles, and

- the accompanying management report as a whole provides an appropriate view of the Company's position. In all material respects, this management report is consistent with the annual financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our audit opinion on the management report does not cover the content of those parts of the management report listed in the "Other Information" section of the management report.

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

Basis for the Audit Opinions

We conducted our audit of the annual financial statements and of the management report in accordance with § 317 HGB and the EU Audit Regulation (No. 537/2014, referred to subsequently as "EU Audit Regulation") and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Our responsibilities under those requirements and principles are further described in the "Auditor's Responsibilities for the Audit of the Annual Financial Statements and of the Management Report" section of our auditor's report. We are independent of the Company in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) point (f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the annual financial statements and on the management report.

Key Audit Matters in the Audit of the Annual Financial Statements

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

In our view, the matter of most significance in our audit is as follows:

- Valuation of the claims reserves

Our presentation of this key audit matter has been structured as follows:

- Matter and issue

- Audit approach and findings

- Reference to further information

Hereinafter we present the key audit matter:

- Valuation of the underwriting reserves

- Matter and issue

In the Company's annual financial statements, under the balance sheet item "Reserve for insurance claims not yet settled", the underwriting reserves (referred to as "claims reserves") are stated at an amount of EUR 47,883 thousand (46.9% of the balance sheet). The methodology and calculation parameters applied in determining the level of claims reserves are based on the discretionary decisions and assumptions of the executive directors. Minor changes to these assumptions and the methodology applied can have a substantial effect on the valuation of the claims reserves. Due to the material importance of the level of these reserves for the net assets and results of operations of the Company as well as the considerable discretionary powers of the executive directors and the associated estimation uncertainties, the valuation of the claims reserves was of particular importance in the context of our audit.

- Audit approach and findings

In light of the importance of the claims reserves for the Company's overall business, as part of our audit and together with our internal valuation specialists, we assessed the methodology used by the Company and the assumptions made by its executive directors. In doing so, we relied on our knowledge and experience of the industry and also took recognized methods into consideration. Furthermore, we observed the structure and effectiveness of the controls established by the Company for determining and recording claims reserves. Working on this basis, we carried out additional analytical audit procedures and tests of details in relation to the valuation of the claims reserves. Among other things, we compared the data underlying the calculation of the settlement amount against the basic documentation. Together with this, we reconstructed the sums calculated by the Company for the level of claims reserves applying the applicable legal requirements and assessed the consistent application of the valuation methods and the allocation of revenues and expenses to the relevant accounting period. Based on our audit procedures, we were able to assure ourselves that the estimations and assumptions made by the executive directors for the valuation of the claims reserves are justified and sufficiently documented.

- Reference to further information

The statements of the Company about the valuation of the claims reserves are contained in the section "Accounting and Measurement Policies" in the notes to the financial statements.

Other Information

The executive directors are responsible for the other information.

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

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

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

- is materially inconsistent with the annual financial statements, with the management report or our knowledge obtained in the audit, or

- otherwise appears to be materially misstated.

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

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

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

Furthermore, the executive directors are responsible for the preparation of the management report that as a whole provides an appropriate view of the Company's position and is, in all material respects, consistent with the annual financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In addition, the executive directors are responsible for such arrangements and measures (systems) as they have considered necessary to enable the preparation of a management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the management report.

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

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

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

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

We exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the annual financial statements and of the management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our audit opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

- Obtain an understanding of internal control relevant to the audit of the annual financial statements and of arrangements and measures (systems) relevant to the audit of the management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an audit opinion on the effectiveness of these systems of the Company.

- Evaluate the appropriateness of accounting policies used by the executive directors and the reasonableness of estimates made by the executive directors and related disclosures.

- Conclude on the appropriateness of the executive directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the annual financial statements and in the management report or, if such disclosures are inadequate, to modify our respective audit opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to be able to continue as a going concern.

- Evaluate the overall presentation, structure and content of the annual financial statements, including the disclosures, and whether the annual financial statements present the underlying transactions and events in a manner that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Company in compliance with German Legally Required Accounting Principles.

- Evaluate the consistency of the management report with the annual financial statements, its conformity with German law, and the view of the Company's position it provides.

- Perform audit procedures on the prospective information presented by the executive directors in the management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by the executive directors as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate audit opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

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

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

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

OTHER LEGAL AND REGULATORY REQUIREMENTS

Further Information pursuant to Article 10 of the EU Audit Regulation

We were elected as auditor by the supervisory board on 8 November 2017. We were engaged by the chairman of the supervisory board on 8 November 2017. We have been the auditor of SOVAG, Hamburg, without interruption since the financial year 2012.

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

GERMAN PUBLIC AUDITOR RESPONSIBLE FOR THE ENGAGEMENT

The German Public Auditor responsible for the engagement is André Bödeker.

PUBLISHING DETAILS

Published by
Schwarzmeer und Ostsee Versicherungs-Aktiengesellschaft SOVAG
Hohe Bleichen 11
D-20354 Hamburg
Phone +49 40 22 71 28-0
Fax +49 40 22 71 28-550

Web www.sovag.de
Email info@sovag.de

Hamburg District Court HRB 3560
Vat-No. DE118617614

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SOVAG
Schwarzmeer und Ostsee
Versicherungs-AG
Hohe Bleichen 11
20354 Hamburg, Germany
www.sovag.de