

## Report of the Supervisory Board



Dr Bernd Flohr (Chairman of the Supervisory Board)

Following the conversion of KSB Aktiengesellschaft into a partnership limited by shares (KGaA) [*Kommanditgesellschaft auf Aktien*], which was decided at the Annual General Meeting on 10 May 2017 and became effective on 17 January 2018, KSB SE & Co. KGaA, Frankenthal (Pfalz), (hereinafter referred to as the “company” or “KSB”) can now look back on almost an entire year in the new legal form. The management is the responsibility of the general partner, KSB Management SE, Frankenthal (Pfalz), acting through its Managing Directors. After the change in legal form, the Supervisory Board continued to extensively monitor the position and development of the company. We performed our tasks as set out by the law, the Articles of Association and the Rules of Procedure with the greatest of diligence. We advised the general partner on corporate management issues and monitored its work. The Managing Directors informed us about current developments, including but not limited to the company’s business, financial and staffing situation, planned investments, corporate planning and strategy via written and oral reports prepared regularly and on an ad hoc basis in a comprehensive and timely manner. We met regularly to discuss selected issues without the Management.

We discussed all business transactions which were significant for the company in depth on the basis of reports from the Managing Directors. Any departures in business developments from the plans and targets were explored by us and commented on in detail by the Managing Directors. The Supervisory Board involved external consultants in the treatment and assessment of special matters, and all decisions made by the Supervisory Board were based on thorough review and consultation. Beyond the intensive work in plenary sessions and in the committees, the Chairman of the Supervisory Board in particular and other members of the Supervisory Board

were in constant contact with the Managing Directors. There was a regular exchange of information with the Administrative Board of KSB Management SE, including but not limited to its Chairman, on current business developments and significant transactions, as well as on questions of strategy, planning, risk situations, risk management and compliance. The Chairman of the Administrative Board also took part in some of the Supervisory Board meetings. The Chairman of the Supervisory Board and his deputy were guests of the Administrative Board on selected issues.

Conflicts of interest of the Supervisory Board members Klaus Kühborth and Monika Kühborth within the scope of the relations covering the supply of services of KSB AG to its majority shareholder, Johannes und Jacob Klein GmbH, Frankenthal (Pfalz), as well as to other related parties, as discussed in the previous year's report, have been disclosed to the Supervisory Board; both did not participate in discussions and the taking of resolutions on this subject area. In the reporting period, no other conflicts of interest arose involving members of the Supervisory Board or the Management that would have been subject to disclosure in the Report of the Supervisory Board.

### **Main Focus of Work in the Supervisory Board Plenary Sessions**

In the 2018 financial year ("year under review"), four regular Supervisory Board meetings and a constituent meeting were held; in addition, the Supervisory Board met twice to discuss special topics. The performance of the company and the KSB Group was the subject of regular discussions, with a particular focus on their business and employment situation, major investment projects and the strategic direction.

Key topics of our consultations with the Managing Directors were the analysis of business developments in the different segments and regions and the company's economic position. Suitable measures to improve the net assets, financial position and results of operations and risk provisioning for major projects, and the growth initiatives presented by the Managing Directors were discussed. The Supervisory Board received regular reports on measures to increase efficiency, including expanding the group-wide shared services activities and harmonising the international accounting processes. The Managing Directors also provided information on the development of ongoing major investments in our production facilities at various sites, and on their completion, where applicable. For example, work on the second expansion phase of our new factory in Shirwal, India, is progressing well and the halls completed in the first expansion phase are already showing high capacity utilisation levels. The Supervisory Board was also involved in the decision on the acquisition of the US service company Dubric; the primary aim is that it will contribute to a stronger presence for the KSB range of services in the American Midwest. In line with the recommendations and suggestions of the German Corporate Governance Code, we looked into fundamental aspects of good corporate governance, which in the year under review included assessing the efficiency of the work of the Supervisory Board. Special emphasis was placed on the further development of our corporate culture; there are various initiatives which aim to help ensure that KSB is in a good position in the challenging competition for specialists and young talent.

Topics discussed at the individual Supervisory Board meetings included the following:

The meeting in **March 2018** focused on the audit and approval of the annual financial statements for the 2017 financial year, including the management report and the combined separate non-financial report for KSB and the KSB Group in accordance with Sections 315b, 315c and 289c to 289e HGB [*Handelsgesetzbuch* – German Commercial Code] (“non-financial report”); the auditors explained the key audit areas and results. The Chairman of the Audit Committee produced an extensive report on the audit carried out on accounting processes for the period. We agreed to the proposal on the appropriation of the net retained earnings presented by the general partner for the 2017 financial year.

In **May 2018**, we consulted on the current business situation and discussed in detail the risk provisioning for a major project in Great Britain which includes the supply of pumps for a deep waste water tunnel in London. The agenda included the progress on preparations for the certification of a newly developed large pump for the Chinese energy market and the potential for follow-up orders. A successful market launch for this kind of pump would strengthen KSB’s position there on a sustainable basis. Given the increasing significance of digital technologies, the Supervisory Board was also informed about the business models which have already been successfully implemented by KSB, and promising future opportunities.

The **September meeting** of the Supervisory Board was held at the Pegnitz site in Bavaria, Germany. The site manager and the Managing Directors reported on the financial situation at the factory there. We were able to gain our own impressions of the recent investments to modernise the foundry and of other production facilities at the site, which confirmed the high level of technical development of the plant. Our valves business was another subject of extensive discussion, as this market is much more fragmented than that for pumps. The planned project to review the company’s strategic direction, which will come into focus in the current 2019 financial year, was also discussed. The agenda for the September meeting also included the concept for the review of the efficiency of the Supervisory Board’s work, in the form of a self-evaluation which was subsequently implemented.

As well as the report on specific measures with impact on income in the 2018 financial year, the **December meeting** focused on planning for the 2019 financial year. The ways in which KSB can achieve the planned growth and increase profitability were presented in detail by the Managing Directors, including the basic methodological and strategic considerations.

In the **two special meetings** of the Supervisory Board, in particular, we covered the status on reviewing the company’s supply of services to its majority shareholder and other related parties. The relevant issues were clarified with the assistance of external solicitors and tax consultants. After preparation by the Audit Committee, they supported the Supervisory Board with the in-depth consultation and mandatory review of potential claims by the company and their assertion. Significant compensation payments for services which were not sufficiently remunerated were demanded from the relevant recipients of the services, and these were also paid.

We additionally decided to assert claims against individual former members of the Board of Management and have taken the necessary steps to do this.

### Main Focus of Work in the Committees

In order to perform its duties efficiently, the Supervisory Board worked with four committees during the year under review. These prepared the Supervisory Board's resolutions and the special topics to be discussed in the plenary sessions. In addition, they also made their own decisions – to the extent legally permissible – within the scope of their areas of responsibility. This allocation has proved worthwhile in practice. The Chairs of the committees regularly and comprehensively reported in the plenary sessions on the content and results of the work carried out in the committees.

The **Nomination Committee** prepared proposals for the appointment of shareholder representatives to the Supervisory Board, for example the Supervisory Board's nominations for the election of Supervisory Board members by last year's Annual General Meeting. It met once during the year under review. In looking for and evaluating suitable candidates with the requisite expertise and experience of the industry, long-term succession planning is a key factor.

#### SUPERVISORY BOARD COMMITTEES

and their Chairs, as well as number of meetings in the year under review

##### CORPORATE DEVELOPMENT COMMITTEE

Until 31 Jan. 2018  
Oswald Bubel  
From 21 March 2018  
Klaus Kühborth  
Meetings: 4

##### NOMINATION COMMITTEE

Dr Bernd Flohr,  
Klaus Kühborth  
Meetings: 1

##### PERSONNEL COMMITTEE

Dr Bernd Flohr  
Meetings: 3

##### AUDIT COMMITTEE

Klaus Burchards  
Meetings: 9

The **Corporate Development Committee** deals with the strategic development in the fields of technology, production and sales, among other things. It had four meetings in the year under review. The opportunities presented by digitalisation were discussed in depth with a view to establishing and expanding relevant business models in order to leverage the potential with our customers and along our own value creation chain. Against the backdrop of the continued relevance of energy efficiency, the Committee dealt with drive technology and the increasing use of mechatronic solutions. The agenda also included considerations on the flexible use of manufacturing capacities so far reserved for serving the energy market. There was also extensive discussion of special sales initiatives in individual sales markets. These include the food and beverage industries, which have been recording high rates of growth. The pumps and valves employed in the production facilities in these industries have to comply with strict hygiene requirements and allow gentle transport of fluids. The Committee also heard reports on current strategic developments. The Managing Directors and the managers of the specialist departments responsible regularly attended the Committee meetings.

The **Personnel Committee** held three meetings in the year under review. It focuses on subjects and challenges relating to Human Resources activities within the Group. It also decides on the approval of any internal transactions with KSB Management SE, its Administrative Board members and/or its Managing Directors, on the consent to other activities of these persons, the granting of loans to them and on any matters related to the remuneration of the Supervisory Board members. In the year under review, the Committee discussed with the specialist department responsible the plan for and the approach to the group-wide introduction of personnel administration and management software as well as measures to further improve the corporate culture and employer attractiveness. It also reviewed and approved agreements for the provision and billing of services by the company to KSB Management SE.

The nine meetings of the **Audit Committee** during the year under review were generally attended by the Managing Directors involved and the managers of the relevant specialist departments, plus, on multiple occasions, the auditors. The Audit Committee discussed the 2017 annual and consolidated financial statements and the relevant audit reports submitted by the auditors. The non-financial report was also discussed in detail. The Committee prepared the independent examination by the Supervisory Board of the financial statements, the management reports and the proposal on the appropriation of the net retained earnings. The Committee also discussed the half-year financial report for the year under review with the Managing Directors. In addition, the Audit Committee submitted a recommendation for the selection of auditors by last year's Annual General Meeting to the plenary session. The Audit Committee commissioned the auditors with auditing the annual and consolidated financial statements for the 2018 financial year and defined specific key areas for the audit. The declaration of independence by the auditors was obtained in accordance with the recommendations of the German Corporate Governance Code (Section 7.2.1), and the auditors' continued independence and performance of non-audit services were monitored. The Committee also focused on monitoring accounting, the accounting process, the risk management system – taking into account the relevant reports from Internal Audits – and the effectiveness of the internal control and auditing system, includ-

ing compliance and the auditing of the annual financial statements. In this context, the Committee dealt in detail with the company's supply of services to its majority shareholder and other related parties and prepared decisions in this respect to be put forward to the Supervisory Board. The agenda also included projects with a material impact on the net assets, financial position and results of operations as well as measures to increase efficiency.

### Corporate Governance and Statement of Compliance

The Supervisory Board continuously monitored developments in corporate governance standards throughout the year under review. The general partner, acting through its Managing Directors, and the Supervisory Board reported on corporate governance at KSB in accordance with Section 3.10 of the German Corporate Governance Code as part of the Corporate Governance Statement pursuant to Sections 289f (2 and 3) and 315d HGB. On 13 March 2019 they issued a joint updated Statement of Compliance in accordance with Section 161 AktG [*Aktiengesetz* – German Public Companies Act] and made it permanently available to shareholders on the company's web site. The company complied with the German Corporate Governance Code's recommendations subject to a few justified exceptions.

### Audit of the 2018 Annual and Consolidated Financial Statements

The Supervisory Board examined the annual financial statements and the management report of KSB SE & Co. KGaA for the year ended 31 December 2018, which were prepared in accordance with the provisions of the *Handelsgesetzbuch* (HGB), as well as the consolidated financial statements and the Group management report for the year ended 31 December 2018, which were prepared in accordance with the International Financial Reporting Standards (IFRSs), and the proposal by the general partner on the appropriation of the net retained earnings. This also applies to the non-financial report.

PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, based in Frankfurt am Main with an office in Mannheim, audited the annual financial statements and the management report of KSB SE & Co. KGaA for the year ended 31 December 2018, as well as the consolidated financial statements and the Group management report for the year ended 31 December 2018, and issued an unqualified opinion for each. The key audit areas defined for the auditors by the Audit Committee for the year under review mainly included the annual impairment test for goodwill and property, plant and equipment in the consolidated financial statements as well as the reporting on and presentation of transactions with related parties in the single-entity financial statements. The non-financial report was reviewed. The auditors reported on their findings on these key audit areas both orally and in writing.

The accounting documentation, the proposal by the general partner on the appropriation of the net retained earnings, the non-financial report and the audit reports submitted by the auditors were provided in good time to all members of the Supervisory Board. They were discussed in detail by the Audit Committee, especially on 13 March 2019, as well as in the

Supervisory Board plenary session on 20 March 2019, and explained in depth by the Managing Directors of the general partner. The auditors attended the meetings of both bodies, reported on the findings of the audit and were available to provide additional information.

The Supervisory Board concurs with the auditors' findings. Following the final result of the examination by the Audit Committee and its own review, the Supervisory Board raised no objections to the annual financial statements, consolidated financial statements, management report and Group management report, as well as the non-financial report. In accordance with the recommendation of the Audit Committee, the Supervisory Board approved the annual financial statements prepared by the general partner. The proposal of the general partner on the appropriation of the net retained earnings of KSB SE & Co. KGaA, and in particular the reduction of the dividend to € 3.00 per ordinary no-par-value share and € 3.38 per preference no-par-value share, is deemed to be appropriate by the Supervisory Board in accordance with its own review; it concurs with the proposal.

### Dependent Company Report

The general partner was obliged to produce a dependent company report in accordance with Section 312 AktG until the new legal form became effective on 17 January 2018. This obligation no longer applies for the period starting on the effective date of the change of legal form. However, KSB decided to prepare this report beyond the statutory period for the full 2018 financial year in order to review and document the effectiveness of the measures taken in relation to business with dependent companies. The report was reviewed by the auditors, who issued the following unqualified opinion:

“On completion of our audit and assessment in accordance with professional standards, we confirm that

1. The actual amounts and disclosures in the report are correct.
2. The consideration paid by the company for the transactions listed in the report was not inappropriately high.”

The report of the general partner and the audit report were provided in good time to all members of the Supervisory Board and were also discussed by the Audit Committee and in plenary sessions. The auditors attended the meetings of both bodies, reported on the material findings of the audit and were available to provide additional information. The Supervisory Board concurs with the auditors' findings. Both the recommendation by the Audit Committee and the final results of the Supervisory Board plenary session's examination did not give rise

to any objections to the dependent company report prepared by the general partner and to the statement by the general partner at the end of the dependent company report.

### Changes in the Supervisory Board and the Management

In the year under review, Monika Kühborth and Oswald Bubel resigned from their office as members of the Supervisory Board as of the end of January in order to focus on their responsibilities in the Administrative Board of KSB Management SE. In their place, Arturo Esquinca and Prof. Dr.-Ing. Corinna Salander were appointed to the Supervisory Board first by order of the *Amtsgericht* [Local Court] Ludwigshafen am Rhein on 26 February 2018 and then by the Annual General Meeting on 16 May 2018. Following the results of the election of new employee representatives to the Supervisory Board, the Annual General Meeting on 16 May 2016 appointed Thomas Pabst and Claudia Augustin in place of the departing Dr H. Stefan Wiß and Wolfgang Kormann. At a constituent Supervisory Board meeting which immediately followed the Annual General Meeting, Dr Bernd Flohr was confirmed in his office as Chairman of the Supervisory Board and Alois Lautner in his office as Deputy Chairman.

The Supervisory Board would like to thank the Managing Directors and the Administrative Board of the general partner, the employees and employee representatives of all Group companies for their continued constructive and committed work during the past financial year.

Frankenthal, 20 March 2019

The Supervisory Board