

Corporate Governance

Report of the Supervisory Board

Dear Shareholder,

In the following, the Supervisory Board reports on its work and that of its committees in the 2017 fiscal year: We closely supervised, carefully monitored and advised the Executive Board in the management of the company. We comprehensively fulfilled all the tasks incumbent upon us under applicable law, the Articles of Incorporation and our By-Laws. We have satisfied ourselves of the legality and expediency of management. We were directly involved in a timely manner in all decisions of fundamental importance to the company.

The Executive Board provided the Supervisory Board with regular, timely and comprehensive updates in writing and verbally on all issues of relevance to the company. In particular, these include planning, business strategy, significant business transactions in the company and the corporation, and the related risks and opportunities, as well as compliance issues. The Executive Board continually informed the Supervisory Board in detail of the sales, results and employment development in the corporation and individual divisions as well as the financial situation of the company. Where the actual course of business deviated from the defined plans and targets, the Executive Board provided detailed explanations. It discussed the reasons for these deviations and the measures introduced in depth with the Supervisory Board and its committees. In addition, the Supervisory Board, the Chairman's Committee and the Audit Committee dealt intensively with other key company matters at their meetings and in separate discussions. The members of the Supervisory Board were also available to the Executive Board for consultation outside the meetings. As chairman of the Supervisory Board, I was in regular contact with the Executive Board and its chairman and discussed current company issues and developments with them.

Meetings of the Supervisory Board and the committees

The Supervisory Board held four ordinary meetings in 2017 as well as the strategy meeting and two telephone conferences. At two meetings, the Supervisory Board conferred part of the time in the absence of the Executive Board; one telephone conference took place entirely without the Executive Board. The Chairman's Committee held two meetings and two telephone conferences in the year under review. The Audit Committee met four times in 2017. The Nomination Committee held a written vote on the proposal of a profile of skills and expertise for the Supervisory Board and in one meeting approved a proposal for naming the independent shareholder representatives (see also Corporate Governance Report, page 20). The Mediation Committee in accordance with Section 27 (3) of the German Co-determination Act (*Mitbestimmungsgesetz - MitbestG*) did not need to meet. There are no other committees. All committees report to the plenary session on a regular basis. The Corporate Governance Report starting on page 18 describes their responsibilities in more detail and names their members.

Most members of the Supervisory Board attended all meetings in person. All members of the Supervisory Board attended more than half of the meetings of the plenary session and the committees,

respectively, to which they belonged in the past fiscal year. A detailed account of each Supervisory Board member's meeting attendance will be published in the Investors section of our website [📄](#) on March 21, 2018, with the invitation to the Annual Shareholders' Meeting.

Key topics dealt with by the Supervisory Board and the Chairman's Committee

The Supervisory Board's discussions repeatedly focused on the company's strategic development and orientation. At the strategy meeting in particular, the Executive Board and the Supervisory Board once again discussed at length the strategic objectives and strategic planning of the corporation and the divisions and the HR strategy. In addition, the Executive Board presented the preliminary results of the review of the strategy of the Powertrain division in a separate telephone conference in April 2017.

Other key topics of the strategy meeting were developments in Industry 4.0 and cybersecurity, which will be of vital importance both for automated driving and for the increasing interconnectivity of vehicles. Continental has expanded its expertise considerably in this respect by acquiring Argus Cyber Security Ltd, Tel Aviv, Israel, one of the world's leading companies in this field. After in-depth discussion by the plenary session, the Supervisory Board approved this transaction at its meeting in September 2017 and further Chairman's Committee proceedings. The acquisition of an indirect stake in HERE International, B.V., Amsterdam, Netherlands, announced in January 2018 in conjunction with the conclusion of a cooperation agreement is an important step toward generating additional profitable growth in the field of mobility services and automated driving. This project was also approved by the Supervisory Board at its September meeting.

As always, in addition to the situation on the raw materials and sales markets, the share-price performance was a regular subject of the discussions in the Executive Board's reporting on the current business development. Moreover, the Supervisory Board discussed further management actions by the Executive Board that require the approval of the Supervisory Board or its Chairman's Committee in accordance with the company's Articles of Incorporation and the Supervisory Board By-Laws. After careful examination, approval was granted for investment projects of the Chassis & Safety and Tire divisions. Other issues that the Supervisory Board dealt with in the past fiscal year included the protection of the company's IT systems against external attacks, risk management in the supply chain and cooperation with universities. In its meeting on December 13, 2017, the Supervisory Board discussed the annual planning for 2018 and long-term planning. It also approved the planning and the investment plans for fiscal 2018.

The Supervisory Board regularly reviews the Executive Board's remuneration. The Supervisory Board brought in an independent external consultant to carry out such a review again in 2016. Based on this, in January 2017 the Supervisory Board essentially decided to increase



parts of the variable remuneration but to leave the remuneration system as it is. The details are described in the Remuneration Report starting on page 24. The Annual Shareholders' Meeting on April 28, 2017, approved the Executive Board remuneration system again.

Key topics dealt with by the Audit Committee

The Audit Committee was also informed by the Executive Board in detail and on an ongoing basis about sales, results and employment development in the corporation and individual divisions as well as the financial situation of the company. The Executive Board is assisted by the heads of Accounting and Corporate Controlling, who can provide the Audit Committee directly with information at its meetings. In addition, the chairman of the Audit Committee is in contact with the chief financial officer and the auditor of the corporation outside of the meetings on a regular basis. The Audit Committee likewise ensures that it is regularly informed of the progress of major acquisition and investment projects. In 2017, these included the acquisition of A-Z Formen in the Tire division and of Elektrobot Automotive and Zonar Systems in the Interior division, which were concluded in 2015 and 2016 respectively.

Before the half-year and quarterly financial reports were published, the Audit Committee discussed and reviewed them with the Executive Board, paying particular attention to the results for the

relevant reporting period as well as the outlook for the year as a whole. The interim financial statements as at June 30, 2017, were reviewed by KPMG AG Wirtschaftsprüfungsgesellschaft, Hanover (KPMG), on behalf of the Audit Committee. The Audit Committee also issued the mandate for the audit of the 2017 annual and consolidated financial statements, as well as the Dependent Company Report, to KPMG, pursuant to the resolution adopted by the Annual Shareholders' Meeting. The committee also coordinated key audit matters with the auditor.

The Audit Committee acknowledged that the German Financial Reporting Enforcement Panel (FREP) had concluded its audit of the 2016 financial statements without finding any errors. The Audit Committee also again approved a blanket amount for assigning the auditor non-audit services in accordance with the EU audit regulation. Moreover, the Audit Committee dealt with issues including the process for selecting a new auditor, because a change is required by 2021 at the latest.

A new task for the Audit Committee is the preparation of the review of the company's non-financial reporting by the Supervisory Board, which is required for the first time for the 2017 fiscal year. The responsibility of potentially commissioning an external auditor to audit the content of this reporting was likewise delegated to the Audit Committee. The Audit Committee dealt with questions

arising in connection with this in several meetings. In consultation with the Audit Committee, the Executive Board decided not to supplement the management report with a non-financial declaration but instead to compile a separate non-financial corporate report. The Audit Committee resolved to commission KPMG to review the content of the non-financial corporate report with the aim of an evaluation with limited assurance and issued the mandate for the audit.

The Audit Committee is closely involved in compliance and risk management. The work of the Compliance department and the Corporate Audit department, as well as reporting on significant events are regular topics at each Audit Committee meeting. These included in particular the matters described in more detail in the Report on Risks and Opportunities and in the Notes to the Consolidated Financial Statements. The head of the Compliance department and the head of Corporate Audit were also available to provide information directly to the Audit Committee and its chairman in coordination with the Executive Board. The chairman of the Audit Committee shares key information as part of his regular reporting to the plenary session. In addition, the head of the Compliance department reports directly to the plenary session of the Supervisory Board once a year about the work of the Compliance department and significant compliance cases.

In addition, the Executive Board reported to the Audit Committee on the material risks covered by the risk management system and the corresponding measures resolved. The Audit Committee has satisfied itself of the effectiveness of the internal control system, the risk management system and the internal audit system.

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In several meetings, the Supervisory Board dealt with the amendments to the German Corporate Governance Code that took effect at the end of April 2017. It will follow the new recommendations insofar as they concern the Supervisory Board. The Supervisory Board also accepted the code's suggestion of entering into a direct dialogue with investors on topics specific to the Supervisory Board. As chairman of the Supervisory Board, I therefore conducted a telephone conference with investor representatives in November 2017, in which we discussed topics such as the remuneration of the Executive Board and Supervisory Board, the composition of the Supervisory Board and the Supervisory Board's involvement in the company's strategy. At its meeting in December 2017, the Supervisory Board agreed an updated declaration in accordance with Section 161 of the German Stock Corporation Act (*Aktien-gesetz - AktG*) on the recommendations of the German Corporate Governance Code.

In the year under review, two members of the Supervisory Board withdrew from an informational presentation held by the Executive Board during a meeting in order to avoid any potential conflict of interest. There were no other conflicts of interest from members of the Supervisory Board. In its opinion, the Supervisory Board also had an appropriate number of independent members as defined in the German Corporate Governance Code at all times in the period under review.

Further information on corporate governance is included in the Corporate Governance Report starting on page 18.

Annual and consolidated financial statements; non-financial corporate report

KPMG audited the annual financial statements as at December 31, 2017, prepared by the Executive Board in accordance with the provisions of the German Commercial Code (*Handelsgesetzbuch - HGB*), the 2017 consolidated financial statements, and the summarized management report for the corporation and Continental AG, including the accounts, the accounting-related internal control system, and the system for early risk recognition. The 2017 consolidated financial statements of Continental AG were prepared in accordance with the International Financial Reporting Standards (IFRS). The auditor issued unqualified opinions. In terms of the system for early risk recognition, the auditor found that the Executive Board had taken the necessary measures under Section 91 (2) *AktG* and that the company's system for early risk recognition is suitable for identifying developments at an early stage that pose a risk to the company as a going concern. In addition, KPMG audited the Executive Board's report on relations with affiliated companies pursuant to Section 312 *AktG* (Dependent Company Report). KPMG issued the following unqualified opinion on this report in accordance with Section 313 (3) *AktG*:

"Based on the results of our statutory audit and evaluation we confirm that:

- › the actual information included in the report is correct,
- › with respect to the transactions listed in the report, payments by the company were not unduly high or that detrimental effects had been compensated for, and
- › there are no circumstances in favor of a significantly different assessment than that made by the Executive Board in regard to the measures listed in the report."

The Audit Committee discussed the documents relating to the annual financial statements, including the Dependent Company Report, and the audit reports with the Executive Board and the auditor on February 28, 2018. Furthermore, the plenary session of the Supervisory Board discussed these at length at its meeting to approve the annual financial statements on March 13, 2018. The discussions also concerned the separate non-financial report of the Continental Corporation and of Continental AG according to Section 289b and Section 315b *HGB*. The required documents were distributed to all members of the Audit Committee and the Supervisory Board in good time before these meetings so that the members had sufficient opportunity to review them. The auditor was present at these discussions. The auditor reported on the main results of the audits and was available to provide additional information to the Audit Committee and the Supervisory Board. Based on its own review of the annual financial statements, the consolidated financial statements, the company management report, the combined management report of Continental AG and of the corporation, as well as the Dependent Company Report

including the final declaration of the Executive Board, and based on the report and the recommendation of the Audit Committee, the Supervisory Board concurred with the results of the auditor's audit. There were no objections. The Supervisory Board approved the annual financial statements and the consolidated financial statements. The annual financial statements are thereby adopted. KPMG issued an unqualified opinion for the non-financial corporate report. This means that, based on the implemented audit procedures and the resulting audit report, no matters came to light that would cause KPMG to presume the summarized separate non-financial corporate report has not been prepared, in material respects, in accordance with sections 315b and 315c in conjunction with 289c to 289e of *HGB*. The Supervisory Board also found no reasons arguing against the legality and expediency of the separate non-financial corporate report. This was based on the Supervisory Board's own review, the Audit Committee's recommendation and report on its preliminary examination, and KPMG's opinion and review of the report.

The Supervisory Board together with the Executive Board will propose a dividend distribution of €4.50 per share for the past fiscal year at the Annual Shareholders' Meeting on April 27, 2018.

Personnel changes in the Supervisory Board and Executive Board

In 2017, there were no personnel changes in the Supervisory Board. As of February 28, 2018, Hartmut Meine, who up to that point had been the vice chairman of the Supervisory Board, stepped down to begin his retirement. The Supervisory Board would like to thank Hartmut Meine for his many years of service and for his constructive contribution to the work of the Supervisory Board. The Hanover Local Court (*Amtsgericht*) named Christiane Benner as his successor on February 8, 2018. She is vice president of IG Metall.

Further information on the members of the Supervisory Board and its committees who were in office in the year under review can be found starting on page 19, and on pages 207 and 208.

Dr. Ralf Cramer departed from the Executive Board when his mandate expired on August 11, 2017. The Supervisory Board would like to thank him for his many years of hard work and commitment in various roles within the company, including most recently the very successful development of activities in China. At its meeting in September, the Supervisory Board extended the appointment of Hans-Jürgen Duensing as a member of the Executive Board by another five years until the end of April 2023. At this meeting, the Supervisory Board also dealt thoroughly with succession planning for the Executive Board. With the exception of a presentation by Dr. Ariane Reinhart, these discussions were held in the absence of the Executive Board.

The Supervisory Board would like to thank the Executive Board, all the employees and the employee representatives for their excellent work, which enabled the company to develop well overall in the past year.

Hanover, March 13, 2018

For the Supervisory Board,



Prof. Dr.-Ing. Wolfgang Reitzle
Chairman