

## REPORT OF THE SUPERVISORY BOARD

Throughout the last financial year, the Supervisory Board continued to perform its tasks with great care in accordance with the law, the Articles of Association and the Rules of Procedure. We regularly advised the Board of Management on corporate management issues and monitored its work. The Supervisory Board was consulted directly and at an early stage with regard to decisions of fundamental importance. The Board of Management informed us in a comprehensive and timely manner about the position of the company, in particular its business, financial and staffing situation, planned investments, as well as relevant corporate planning and strategic and organisational development issues via written and oral reports prepared regularly and on an ad hoc basis. We continued to meet on a regular basis to discuss selected issues, both with and in the absence of the Board of Management.

We discussed all business transactions significant for the company in detail on the basis of the Board of Management's reports. Any departures in business developments from the plans and targets were reviewed and commented on in detail by the Board of Management. We adopted our resolutions on the reports and proposals by the Board of Management after thorough examination and discussion. Beyond the intensive work in the plenary sessions and in the committees, the Chairman of the Supervisory Board in particular and other Supervisory Board members were in frequent contact with the Board of Management outside the meetings to discuss the current business development and significant transactions as well as questions of strategy, planning, risk assessment, risk management and compliance.

In the year under review, no conflicts of interest arose involving members of the Board of Management or the Supervisory Board that would have been subject to disclosure in the Report of the Supervisory Board.

### MAIN FOCUS OF WORK IN THE SUPERVISORY BOARD PLENARY SESSIONS AND IN THE COMMITTEES

Core topics of our discussions with the Board of Management were the preparation of the strategy revision and the continued development of the corporate organisation. The analysis of business development in the segments and Regions represented an additional focus, as did major investment projects at various sites. We also dealt on an ongoing basis with the company's economic position and the prospects facing selected markets.

Four regular Supervisory Board meetings were held in financial year 2014. The performance of KSB Aktiengesellschaft and the Group was the subject of regular discussions in the plenary sessions, primarily with regard to order intake, sales revenue, earnings, assets and employment levels as well as the current economic situation, strategy, and investment, divestment and acquisition projects. We examined in detail global service activities and their further expansion. Given the large number of acquisitions in recent years, our focus was on their systematic integration; in a few cases where there were structural difficulties, we decided to approve the Board of Management's proposal to sell the units concerned.

The Board of Management regularly explained to us in detail the ways in which KSB can achieve the planned growth for the coming years, including the underlying methodological and strategic considerations. All investments required to pursue these objectives were subjected to critical analysis before being approved and their implementation was monitored by us. In this context, the Supervisory Board approved further financial resources for the modernisation, in stages, of the foundry at the Pegnitz site in Germany. On several occasions, we reviewed the status of far-reaching expansion work at our US subsidiary GIW Industries, Inc. This project will take several years. In contrast, we expect the new production facilities at our La Roche-Chalais site in France to be commissioned on schedule before the end of the year. In order to obtain a major Chinese order for the supply of pumps, we had to comprehensively expand our local manufacturing facilities, as already reported on several occasions. Following completion of these measures, we received regular updates from the Board of Management on the progress of order processing. Successful implementation of this demanding project will strengthen KSB's market position over the long term. In a number of countries, the start or expansion of business activities led to property acquisitions. In each case we discussed the long-term impact of such measures.

Given the ongoing changes in the energy sector, we continued to look at the impact these radical market movements are having on our business operations. We subjected the deliberations of the Board of Management on this subject to critical scrutiny, focusing in particular on the qualitative assessment of relevant measures and their implementation. The main focus in this regard was the overall optimisation of production capacities within our international manufacturing network.

Repeatedly on the agenda was the development of our corporate organisation. We devoted particular attention to the continuation of the process launched in 2013 to realign our international and worldwide sales activities, bringing them closer into line with our customers' needs. In addition, we tackled the reduction in the number of Group companies; in addition to streamlining the communication paths, we hope this will also lead to lower administrative expenses. Another central focus of our work was the progress made in the continued development of our value-based corporate culture, with the Board of Management providing regular updates. The new staff evaluation and development system presented by the Board of Management in this context will create opportunities for the continuous improvement of performance, at both employee and company level.

In September the Supervisory Board convened for a meeting at the Bremen site. This meeting dealt in detail with the background to the unexpected weakening of the sales revenue and profit figures for the year under review: Both the negative effects of the overall economic environment and considerable non-recurring and restructuring costs played a role. As a result, we advocated a number of measures that we discussed with the Board of Management. Work

to update our strategic objectives, for example, was launched without delay, as a means of ensuring that the latest market developments can be depicted more accurately. At the meeting in Bremen, we also familiarised ourselves with the successful progression of business there and the modern technical plant. We also informed ourselves about selected products and functions of the Group. As mentioned above, at the December meeting we discussed the restructuring of our global production concept; further details will be worked out step by step. We also looked at business performance during the financial year and planning for 2015. In order to streamline the organisational structure of the Supervisory Board itself, we took the step of abolishing the Planning and Finance Committee with effect from the end of the year under review, integrating its remit into the work of the remaining committees. Some of these have been reorganised in terms of their composition and given stronger decision-making powers.

In order to perform its duties efficiently, the Supervisory Board worked with six committees in 2014. These prepare the Supervisory Board's resolutions and the special topics to be discussed in the plenary sessions. In addition, they also make their own decisions – to the extent that this is 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 report in the plenary sessions on the content and results of the work carried out in the committees.

In the run-up to the election at the Annual General Meeting, on 14 May 2014, of new shareholder representatives to the Supervisory Board, the **Nomination Committee** prepared the Supervisory Board's nominations, convening once in the year under review for this purpose. In looking for and evaluating suitable candidates with the requisite expertise and experience of the industry, long-term succession planning is a key factor.

The **Planning and Finance Committee** met four times in the year under review. It focused on corporate and investment planning and the financial situation of the company. Faced with unexpected differences between current business development and the announced goals and targets, the Committee dealt in detail with options available for improving the relevant forecasting processes and for introducing appropriate operational countermeasures. The Committee welcomed the deliberations presented by the Board of Management.

The **Corporate Development Committee** deals with a changing range of key issues. In four meetings in the year under review, it discussed in particular the areas of strategy controlling, production management and innovation, and looked at a number of major investments, including in France and North America. The development of particular markets also figured on the agenda, as did tie-in measures during acquisitions. Questions in relation to the strategy revision were discussed. Talks continued on the optimised and reliable supply of castings to our production sites and on accompanying the measures initiated for this purpose. The heads

## COMMITTEES OF THE SUPERVISORY BOARD

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

### PLANNING AND FINANCE COMMITTEE

Dr. Martin Auer  
No. of meetings: 4

### MEDIATION COMMITTEE

Klaus Kühborth  
No. of meetings: 0

### CORPORATE DEVELOPMENT COMMITTEE

Dr. Hermann Nestler (until 14 May 2014)  
Dr. Thomas Seeberg (until 17 Sep. 2014)  
Klaus Kühborth (until 31 Dec. 2014)  
No. of meetings: 4

### AUDIT COMMITTEE

Dr. Thomas Seeberg  
No. of meetings: 4

### PERSONNEL COMMITTEE

Klaus Kühborth  
No. of meetings: 4

### NOMINATION COMMITTEE

Prof. Dr. Michael Hoffmann-Becking  
No. of meetings: 1

of the relevant specialist departments frequently took part in the committee meetings, along with the responsible members of the Board of Management.

The **Personnel Committee** held four meetings in the year under review. It primarily addresses topics relating to the Board of Management's remuneration, including the terms of the individual service contracts, as well as other Board of Management issues. Decisions on the Board of Management's remuneration are made in plenary session with the committee acting in a preparatory capacity. In addition, the committee discussed staff development issues with the aim of prioritising the recruitment of candidates for the Board of Management and other management positions from within the company's own ranks. In 2014, the committee members again participated in events with staff from various management levels in an effort to foster a direct exchange of ideas. Account was also taken in this regard of the now greater entrepreneurial focus of the management level immediately below the Board of Management.

The four meetings of the **Audit Committee** were always attended by the Member of the Board responsible for Finance and, on several occasions, by the auditors. The committee primarily examined the 2013 annual and consolidated financial statements, the audit reports submitted by the auditors and the internal auditors, and the effectiveness and further development of the risk management system and compliance organisation. In particular, 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. In this context, it also defined key audit areas for the external auditing of the 2014 financial statements. In addition, the 2014 half-year financial report was discussed with the Board of Management. The committee submitted a proposal to the plenary session for the selection of auditors by the 2014 Annual General Meeting and commissioned them to carry out the audit of the

annual and consolidated financial statements for the 2014 financial year. The declaration of independence by the auditors was obtained in accordance with section 7.2.1 of the German Corporate Governance Code and the auditors' continued independence was monitored. During the auditor selection process for the current financial year, the committee reviewed the offers submitted and then made its recommendation to the Supervisory Board for the election of the auditor by the Annual General Meeting. The committee also discussed the monitoring of the financial reporting process and the effectiveness of the internal control and auditing system.

There was no requirement during the financial year under review to convene the **Mediation Committee** required by section 27(3) of the *MitbestG* [*Mitbestimmungsgesetz* – German Co-Determination Act].

### **CORPORATE GOVERNANCE AND STATEMENT OF COMPLIANCE**

The Supervisory Board continuously monitored developments in corporate governance standards throughout the financial year. The Board of Management and the Supervisory Board report 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 section 289a of the *HGB* [*Handelsgesetzbuch* – German Commercial Code]. On 17 September 2014 they issued a joint updated statement of compliance in accordance with section 161 of the *AktG* [*Aktiengesetz* – German Public Companies Act] and made it permanently available to shareholders on the company's web site. KSB Aktiengesellschaft complies with the Code's recommendations subject to a few exceptions.

### **AUDIT OF THE 2014 ANNUAL AND CONSOLIDATED FINANCIAL STATEMENTS**

The accounting documentation, in addition to the proposal by the Board of Management on the appropriation of net retained earnings and the audit reports submitted by the auditors, was provided in good time to all members of the Supervisory Board. The documents were examined in detail by the Audit Committee on 17 March 2015 as well as by the Supervisory Board plenary session on 25 March 2015 and explained in depth in both cases by the Board of Management. 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 examined the annual financial statements and the management report of KSB Aktiengesellschaft for the year ended 31 December 2014, which were prepared in accordance with the provisions of the *Handelsgesetzbuch* [*HGB* – German Commercial Code], as well as the consolidated financial statements and the group management report for the year ended 31 December 2014, which were prepared in accordance with the International Financial Reporting Standards (IFRSs), and the proposal by the Board of Management on the appropriation of net retained earnings.

The Frankfurt am Main office of BDO AG Wirtschaftsprüfungsgesellschaft, Hamburg, audited the annual financial statements and the management report of KSB Aktiengesellschaft for the year ended 31 December 2014, as well as the consolidated financial statements and the Group management report for the year ended 31 December 2014, and issued an unqualified auditors' opinion. The key audit areas defined for the auditors by the Audit Committee for the year under review were: verification of impairment testing for financial investments and goodwill, particularly the validity of the measurement assumptions, and the proper accounting and presentation of restructuring measures. The auditors reported their findings on these key audit areas both orally and in writing.

The Supervisory Board concurs with the auditors' findings. Based on its own final examination results, the Supervisory Board plenary session did not raise any objections to the annual financial statements, consolidated financial statements, management report and Group management report. In accordance with the recommendation of the Audit Committee, the Supervisory Board approved the financial statements prepared by the Board of Management; the annual financial statements are thus adopted. After its own examination, the Supervisory Board deems the proposal by the Board of Management on the appropriation of net retained earnings of KSB Aktiengesellschaft, and in particular the reduced dividend following the significantly lower net profit for the year, to be appropriate and concurs with it.

### DEPENDENT COMPANY REPORT

The auditors also audited the dependent company report for the 2014 financial year prepared by the Board of Management in accordance with section 312 of the *AktG* and issued the following unqualified audit opinion on this report:

“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 reports by the Board of Management and the auditors were provided in good time to all members of the Supervisory Board and were also discussed by the Audit Committee and at 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 Board of Management and to the statement by the Board of Management at the end of the dependent company report.

## CHANGES ON THE BOARD OF MANAGEMENT AND SUPERVISORY BOARD

The long-standing Chair of the Board of Management, Dr. Wolfgang Schmitt, retired as planned on 30 June 2014. Dr. Hermann Nestler resigned from the Supervisory Board at the end of last year's Annual General Meeting, having reached the age limit. The Annual General Meeting elected Dr. Jost Wiechmann to succeed him. Ms Sigrid Maurer also retired from the Supervisory Board with effect from 31 December 2014 following many years' service. Ms Birgit Mohme was appointed a member of the Supervisory Board in her place by order of the *Amtsgericht* (Local Court) Ludwigshafen on 10 December 2014, effective as of 1 January 2015. The Supervisory Board would like to thank the retiring members for their many years of close cooperation.

The Supervisory Board would once again like to thank the Board of Management, the employees and employee representatives of all Group companies for their constructive and committed work in the year under review.

Frankenthal, 25 March 2015

**The Supervisory Board**