

In addition, BASF is a lessee under operating lease contracts. The lease commitments totaling €1,410 million in 2017 (2016: €1,513 million) are due in the following years:

Commitments from operating lease contracts (million €)

	Nominal value of the future minimum lease payments	
	Dec. 31, 2017	Dec. 31, 2016
Less than 1 year	362	360
1-5 years	728	757
More than 5 years	320	396
Total	1,410	1,513

Future minimum lease payments from subleasing contracts based on existing agreements amounted to €10 million in 2017 (2016: €12 million).

In 2017, minimum lease payments of €448 million (2016: €446 million) were included in income from operations. In 2017, conditional lease payments of €1 million (2016: €1 million) were also included in income from operations. Furthermore, sublease payments of €3 million were included in income from operations in 2017 (2016: €4 million).

BASF as lessor

BASF acts as a lessor for finance leases to a minor extent only. Receivables on finance leases were €29 million in 2017 (2016: €33 million).

In 2017, claims arising from operating leases amounted to €93 million (2016: €89 million).

Future minimum lease payments to BASF from operating lease contracts (million €)

	Nominal value of the future minimum lease payments	
	Dec. 31, 2017	Dec. 31, 2016
Less than 1 year	19	17
1-5 years	50	49
More than 5 years	24	23
Total	93	89

Other explanatory notes

29 Statement of cash flows and capital structure management

Statement of cash flows

Cash provided by operating activities contained the following payments:

Million €	2017	2016
Income tax payments	2,147	1,495
Interest payments	409	459
Dividends received	498	225

Interest payments comprised interest payments received of €161 million (2016: €156 million) and interest paid of €570 million (2016: €615 million).

In 2017, BASF SE transferred securities in the amount of €500 million to BASF Pensionstreuhand e.V., Ludwigshafen, Germany. This transfer was not cash effective and therefore had no effect on the statement of cash flows.

In 2016, cash provided by operating activities included €262 million in pension benefits paid, which are covered by a contractual trust arrangement.

Cash used in investing activities included €150 million in payments made for acquisitions (2016: €2,828 million). In the previous year, payments had especially been made for the acquisition of the global surface treatment provider Chemetall from Albemarle Corp., Charlotte, North Carolina.

Payments of €177 million were received for divestitures in 2017 (2016: €664 million). In the previous year, payments had been received primarily from the sale of the Coatings division's industrial coatings business to the AkzoNobel Group and from the sale of the global polyolefin catalysts business to W.R. Grace & Co., Columbia, Maryland.

The payments made for property, plant and equipment, and intangible assets in the amount of €3,996 million included investments for 2017, to the extent that they already had an effect on cash.

Cash and cash equivalents were not subject to any utilization restrictions, as in the previous year.

For more information on cash flow from acquisitions and divestitures, see Note 2.4 from page 187 onward

Reconciliation according to IAS 7 (million €)

	31.12.2016	Cash-effective in cash provided by/used in financing activities	Non-cash effective changes				31.12.2017
			Acquisitions/ divestitures/ changes in the scope of consolidation	Currency effects	Other effects	Changes in fair value	
Financial indebtedness	16,312	2,330	4	(631)	17	–	18,032
Loan liabilities	357	(4)	29	(6)	–	–	376
Liabilities from finance leases	106	(31)	–	(5)	54 ¹	–	124
Other financing-related liabilities	516	542	(23)	(3)	26	–	1,058
Financial and similar liabilities	17,291	2,837	10	(645)	97	–	19,590
Assets/liabilities from hedging transactions	205	411	–	–	–	(734)	(118)
Total	17,496	3,248	10	(645)	97	(734)	19,472

¹ Includes additions from leasing contracts

The reconciliation shows changes in such financial liabilities and hedging transactions for which payments received and made are shown under cash provided by/used in financing activities in the statement of cash flows.

Loan liabilities do not contain any interest components.

Other financing-related liabilities primarily comprise liabilities from accounts used for cash pooling with BASF companies not included in the Consolidated Financial Statements. They are reported in miscellaneous liabilities within the balance sheet item other liabilities which qualify as financial instruments.

The **assets/liabilities relating to hedging transactions** form part of the balance sheet item derivatives with positive or negative fair values and include only those transactions which hedge risks arising from financial indebtedness and financing-related liabilities secured by micro hedges.

For more information on receivables and miscellaneous assets, see Note 18 from page 208 onward

For more information on liabilities, see Note 24 from page 218 onward

Capital structure management

The aim of capital structure management is to maintain the financial flexibility needed to further develop BASF's business portfolio and take advantage of strategic opportunities. The objectives of the company's financing policy are to secure solvency, limit financial risks and optimize the cost of capital.

Capital structure management focuses on meeting the requirements needed to ensure unrestricted access to capital markets and a solid A rating. BASF's capital structure is managed using selected financial ratios, such as dynamic debt ratios, as part of the company's financial planning.

The equity of the BASF Group as reported in the balance sheet amounted to €34,756 million as of December 31, 2017 (December 31, 2016: €32,568 million); the equity ratio was 44.1% on December 31, 2017 (December 31, 2016: 42.6%).

BASF prefers to access external financing on the capital markets. A commercial paper program is used for short-term financing, while corporate bonds are used for financing in the medium and long term. These are issued in euros and other currencies with different maturities. The goal is to create a balanced maturity profile, achieve a diverse range of investors and optimize our debt capital financing conditions.

Currently, BASF has the following ratings, which were most recently confirmed in the fourth quarter of 2017 (Moody's: December 19, 2017; Standard & Poor's and Scope: October 18, 2017).

	Noncurrent financial indebtedness	Current financial indebtedness	Outlook
Dec. 31, 2017			
Moody's	A1	P-1	stable
Standard & Poor's	A	A-1	stable
Scope	A	S-1	stable

	Noncurrent financial indebtedness	Current financial indebtedness	Outlook
Dec. 31, 2016			
Moody's	A1	P-1	stable
Standard & Poor's	A	A-1	stable
Scope	A	S-1	stable

BASF strives to maintain at least a solid A rating, which ensures unrestricted access to financial and capital markets.

For more information on financing policy and the Statement of Cash Flows, see the Management's Report from page 58 onward

30 Share price-based compensation program and BASF incentive share program**Share price-based compensation program**

In 2017, BASF continued its share price-based compensation program known as the long-term incentive (LTI) program for the BASF Group, which has been in place since 1999. Approximately 1,200 people, in particular the Board of Executive Directors and senior executives, are currently eligible to participate in this program. This program provides for the granting of virtual options, which are settled in cash when exercised.

Participation in the LTI program is voluntary. In order to take part in the program, a participant must make a personal investment: A participant must hold BASF shares amounting to 10% to 30% of his or her individual variable compensation for a two-year period from the granting of the option (holding period). The number of shares to be held is determined by the amount of variable compensation and the volume-weighted average market price for BASF shares on the first business day after the Annual Shareholders' Meeting, which was €87.84 on May 15, 2017.

The participant receives four option rights per invested share. Each option consists of two parts, right A and right B, which may be exercised if defined thresholds have been met: The threshold of right A is met if the price of the BASF share has increased by more than 30% in comparison with the base price (absolute threshold). The value of right A is the difference between the market price of BASF shares on the exercise date and the base price; it is limited to 100% of the base price. If the cumulative percentage performance of BASF shares exceeds the percentage performance of the MSCI World Chemicals IndexSM (MSCI Chemicals), right B may be exercised (relative threshold). The value of right B is the base price of the option multiplied by twice the percentage outperformance of BASF shares compared with the MSCI Chemicals Index on the exercise date. It is limited to the closing price on the date of exercise minus the computed nominal value of BASF shares. Beginning with the 2013 LTI program, right B is only valuable if the price of BASF shares at least corresponds with the base price. The options of the LTI program 2017 were granted on July 1, 2017, and may be exercised following a two-year vesting period, between July 1, 2019, and June 30, 2025. During the exercise period, there are certain times (closed periods) during which the options may not be exercised. Each option can only be exercised in full. This means that one of the performance targets must be surpassed. If the other performance target is not surpassed and the option is exercised, the other option right lapses. A participant's maximum gain from exercising an option is limited to five times the original individual investment starting with the 2013 LTI program. The maximum gain from exercising an option is limited to 10 times the original individual investment for programs from previous years. Option rights are nontransferable and are forfeited if the option holders no longer work for BASF or have sold part of their individual investment before the expiry of the two-year vesting period. They remain valid in the case of retirement. For the members of the Board of Executive Directors, the long-term orientation of the program is significantly strengthened compared with the conditions applying to the other participants. The members of

the Board of Executive Directors are required to participate in the LTI program with at least 10% of their actual annual variable compensation. In view of this binding personal investment (in the form of BASF shares), an extended holding period of four years applies. Members of the Board of Executive Directors may only exercise their options at least four years after they have been granted (vesting period).

The 2010 to 2016 programs were structured in a similar way to the LTI program 2017.

The models used in the valuation of the option plans are based on the arbitrage-free valuation model according to Black-Scholes. The fair values of the options are determined using the binomial model.

Fair value of options and parameters used as of December 31, 2017

		LTI program of the year	
		2017	2016
Fair value	€	33.87	41.23
Dividend yield	%	3.38	3.38
Risk-free interest rate	%	0.19	0.05
Volatility BASF share	%	23.63	23.11
Volatility MSCI Chemicals	%	14.22	14.34
Correlation BASF share price: MSCI Chemicals	%	73.41	76.13

The stated fair values and the valuation parameters relate to the LTI programs 2017 and 2016. The fair value calculation was based on the assumption that options will be exercised in a manner dependent on their potential gains. For the programs from preceding years, corresponding fair values were computed and valuation parameters were used.

Volatility was determined on the basis of the monthly closing prices over a historical period corresponding to the remaining term of the options.

The number of options granted amounted to 1,461,113 in 2017 (2016: 1,710,404).

As a result of a resolution by the Board of Executive Directors in 2002 to settle options in cash, options outstanding from the LTI programs 2010 to 2017 were valued with the fair value as of December 31, 2017. A proportionate provision is recorded for programs in the vesting period. The LTI provision decreased from €464 million as of December 31, 2016 to €347 million as of December 31, 2017 due to lower fair values of the outstanding option rights. The utilization of provisions amounted to €49 million in 2017 (2016: €25 million). Income arising from the reversal of provisions amounted to €68 million in 2017. The previous year had included an expense of €267 million.

The total intrinsic value of the exercisable options amounted to €145 million as of December 31, 2017 and €167 million as of December 31, 2016.

BASF incentive share program

The “*plus*” incentive share program was introduced in 1999 and is currently available to employees in Germany, other European countries and Mexico. Simultaneous participation in both the “*plus*” program and the LTI program is not allowed.

Employees who participate in the BASF incentive share program “*plus*” acquire shares in BASF from their variable compensation. For every 10 BASF shares purchased in the program, a participant receives one BASF share at no cost after one, three, five, seven and ten years of holding the BASF shares. As a rule, the first and second block of ten shares entitles the participant to receive one BASF share at no extra cost in each of the next 10 years.

The right to receive free BASF shares lapses if a participant sells the individual investment in BASF shares, if the participant stops working for the Company or one year after retirement. The number of free shares to be granted has developed as follows:

Number of free shares to be granted (shares)

	2017	2016
As of January 1	2,849,723	2,829,521
Newly acquired entitlements	570,465	637,610
Bonus shares issued	(479,111)	(519,984)
Lapsed entitlements	(129,630)	(97,424)
As of December 31	2,811,447	2,849,723

The free shares to be provided by the Company are measured at the fair value on the grant date. Fair value is determined on the basis of the stock price of BASF shares, taking into account the present value of dividends, which are not paid during the term of the program. The weighted-average fair value on the grant date amounted to €86.02 for the 2017 program, and €67.90 for the 2016 program.

The fair value of the free shares to be granted is recognized as an expense with a corresponding increase in capital surplus over the term of the program.

Personnel expenses of €28 million were recorded in 2017 for the BASF incentive share program “*plus*” (2016: €28 million).

31 Compensation for the Board of Executive Directors and Supervisory Board

Million €	2017	2016
Performance-related and not performance-related cash compensation for the Board of Executive Directors	24.8	17.4
Fair value of options granted to the Board of Executive Directors in the fiscal year as of grant date	2.7	4.0
Total compensation for the Board of Executive Directors	27.5	21.4
Service costs for members of the Board of Executive Directors	7.0	3.3
Compensation for the Supervisory Board	3.3	3.0
Total compensation for former members of the Board of Executive Directors and their surviving dependents ¹	7.6	15.9
Pension provisions for former members of the Board of Executive Directors and their surviving dependents	144.3	150.4
Guarantees assumed for members of the Board of Executive Directors and the Supervisory Board	–	–

¹ Compensation for Dr. Harald Schwager and Margret Suckale from their active membership on the Board of Executive Directors in 2017 is included under total compensation for former members of the Board of Executive Directors

Performance-related compensation for the Board of Executive Directors is based on the return on assets adjusted for special effects, as well as the performance of the entire Board. Return on assets corresponds to income before taxes and minority interests plus interest expenses as a percentage of average assets.

The members of the Board of Executive Directors were granted 127,276 options under the long-term incentive (LTI) program in 2017.

The market valuation of the options of active and former members of the Board resulted in income of €5.8 million in 2017. In 2016, the market valuation of the options resulted in expenses of €30.7 million.

For more information on the compensation of members of the Board of Executive Directors, see the Compensation Report from page 140 onward

For more information on the members of the Supervisory Board and Board of Executive Directors, including their memberships on other boards, see page 137 onward

32 Related-party transactions

A related party is a natural person or legal entity which can exert influence on the BASF Group or over which the BASF Group exercises control or joint control or a significant influence. In particular, this comprises nonconsolidated subsidiaries, joint ventures and associated companies.

The following tables show the volume of business with related parties that are included at amortized cost or accounted for using the equity method.

Sales to related parties (million €)

	2017	2016
Nonconsolidated subsidiaries	413	395
Joint ventures	379	317
Associated companies	307	245

Trade accounts receivable from / trade accounts payable to related parties (million €)

	Accounts receivable, trade		Accounts payable, trade	
	December 31, 2017	December 31, 2016	December 31, 2017	December 31, 2016
Nonconsolidated subsidiaries	136	135	77	73
Joint ventures	69	76	75	92
Associated companies	71	55	29	44

Other receivables and liabilities with related parties (million €)

	Other receivables		Other liabilities	
	December 31, 2017	December 31, 2016	December 31, 2017	December 31, 2016
Nonconsolidated subsidiaries	172	176	180	178
Joint ventures	306	196	734	97
Associated companies	73	390	236	258

Sales and trade accounts receivable from and trade accounts payable to related parties mainly included business with own products and merchandise, agency and licensing businesses, and other operating business.

Other receivables and liabilities primarily arose from financing activities, from accounts used for cash pooling, outstanding dividend payments, profit-and-loss transfer agreements, and other finance-related and operating activities and transactions.

The decline in other receivables from associated companies and the increase in other receivables from joint ventures was largely due to the transfer of the financing function for the regulated gas transportation activities to the newly established joint venture W & G Infrastruktur Finanzierungs-GmbH, Kassel, Germany. Receivables from the associated companies GASCADE Gastransport GmbH, Kassel, Germany, and NEL Gastransport GmbH, Kassel, Germany, in the amount of €259 million were transferred to W & G Infrastruktur Finanzierungs-GmbH and a loan of €140 million was granted to it. The cash that was also transferred to the joint venture was deposited in the BASF Group's cash pool and led to an increase of €665 million in other liabilities from joint ventures.

The €22 million decline in other liabilities from associated companies in 2017 was largely due to other financing-related liabilities.

Since the transfer of the global leather chemicals business to the Stahl group on September 29, 2017, BASF holds a minority interest in the parent company of the Stahl group, in which it can exercise significant influence. Sales, receivables, trade accounts receivable and other obligations resulting from transactions with Stahl group since then are included in the tables above in the values for associated companies in 2017.

The outstanding balances toward related parties were generally not secured and settled in cash. The balance of valuation allowances for trade accounts receivable from associated companies rose from €1 million as of December 31, 2016 to €9 million as of December 31, 2017.

Of this amount, €5 million was recognized as an expense in 2017 (2016: €1 million).

The balance of valuation allowances for other receivables from nonconsolidated subsidiaries decreased from €79 million as of December 31, 2016 to €74 million as of December 31, 2017. Of this amount, €1 million was recognized as an expense in 2017 (2016: €26 million).

For more information, see Note 2.3 from page 186 onward

There were obligations from guarantees and other financial obligations at BASF in favor of nonconsolidated subsidiaries in the amount of €5 million as of December 31, 2017 (December 31, 2016: €3 million) and in favor of associated companies in the amount of €23 million as of December 31, 2017 (December 31, 2016: €21 million).

There were no obligations arising from purchase contracts with associated companies as of December 31, 2017; as of December 31, 2016, these amounted to €26 million. Obligations arising from purchase contracts with joint ventures amounted to €3 million as of December 31, 2017, whereas there were no corresponding obligations as of December 31, 2016.

Effective December 31, 2017, the present value of the outstanding minimum rental payments for an office building including parking area payable by BASF SE to BASF Pensionskasse VVaG for the nonterminable basic rental period to 2029 amounted to €55 million.

There were no reportable related party transactions with members of the Board of Executive Directors or the Supervisory Board and their related parties in 2017.

For more information on subsidiaries, joint ventures and associated companies, see the BASF Group List of Shares Held on page 190

For more information on other financial obligations in favor of joint ventures, see Note 25 from page 220 onward

For more information about defined benefit plants, the division of risk between group companies (including non-consolidated subsidiaries), see Note 22, "Provisions for pensions and similar obligations," from page 211 onward

For more information on the members of the Board of Executive Directors and the Supervisory Board, see Management and Supervisory Boards and Compensation Report from page 137 onward

33 Services provided by the external auditor

BASF Group companies have used the following services from KPMG:

Million €	2017	2016
Annual audit	18.6	17.5
Thereof domestic	6.4	6.4
Audit-related services	0.4	0.6
Thereof domestic	0.1	0.3
Tax consultation services	0.2	0.1
Thereof domestic	0.1	–
Other services	0.1	0.3
Thereof domestic	–	0.3
Total	19.3	18.5

The services provided by the external auditor mainly include services for the annual audit, and to a lesser extent, confirmation services, tax consultation services and other services.

The line item annual audit related to expenses for the audit of the Consolidated Financial Statements of the BASF Group as well as the legally required financial statements of BASF SE and its consolidated subsidiary companies and joint opera-

tions. Tax consultation services pertained especially to the fees for the finalization of unfiled tax returns for companies acquired in 2016. Fees for other services primarily included project-related audits in connection with regulatory demands as well as other confirmation services.

34 Declaration of Conformity with the German Corporate Governance Code

Declaration pursuant to section 161 AktG (Stock Corporation Act)

The annual Declaration of Conformity with the German Governance Code according to section 161 of the German Stock

Corporation Act was signed by the Board of Executive Directors and the Supervisory Board of BASF SE in December 2017, and is published online.

For more information, see basf.com/en/governance