

Other Notes

29 Statement of cash flows and capital structure management

Statement of cash flows

Cash flows from operating activities contained the following payments:

Statement of cash flows

Million €	2018	2017
Income tax payments	1,981	2,147
Interest payments	393	409
Dividends received	427	498

In 2018, interest payments comprised interest payments received of €162 million (2017: €161 million) and interest paid of €555 million (2017: €570 million).

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

In 2018, the amount of €134 million was taken from plan assets of BASF Pensionstreuhand e.V., Ludwigshafen am Rhein, Germany, for the reimbursement of pension benefits paid pertaining to 2017.

Cash flows from investing activities included €7,362 million in payments made for acquisitions (2017: €150 million).

Payments of €107 million were received for divestitures in 2018 (2017: €177 million).

Payments made for intangible assets and property, plant and equipment amounted to €3,894 million, €102 million lower than in the previous year.

Cash and cash equivalents in the amount of €2,519 million reported in the statement of cash flows as of December 31, 2018 consist of the balance sheet value (€2,300 million) and the value reclassified to

the oil and gas business disposal group (€219 million). As in the previous year, cash and cash equivalents were not subject to any utilization restrictions.

For more information on cash flows from acquisitions and divestitures, see Note 2.4 from page 205 onward

For more information on the contribution of discontinued operations on BASF's Statement of Cash Flows, see Note 2.5 from page 209 onward

Reconciliation according to IAS 7

Million €							
	Dec. 31, 2017		Non-cash-effective changes				Dec. 31, 2018 ¹
		Cash effective in cash flows from financing activities	Acquisitions/ divestitures/ changes in scope of consolidation	Currency effects	Other effects	Changes in fair value	
Financial indebtedness	18,032	3,252	–	56	11	–	21,351
Loan liabilities	376	150	7	8	–	–	541
Liabilities from finance leases	124	(35)	9	1	35 ²	–	134
Other financing-related liabilities	1,058	(281)	115	(7)	4	–	889
Financial and similar liabilities	19,590	3,086	131	58	50	–	22,915
Assets/liabilities from hedging transactions	(118)	(120)	–	–	–	303	65
Total	19,472	2,966	131	58	50	303	22,980

¹ Contributions as of December 31, 2018 include contributions reclassified to the disposal group and therefore deviate from balance sheet values.

² Includes additions from leasing contracts

The reconciliation breaks down the changes in financial and similar liabilities and their hedging transactions into cash-effective and non-cash-effective changes. The cash-effective changes presented above correspond to the figures in cash flows from financing activities.

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 that qualify as financial instruments.

The **assets/liabilities from 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 235 onward

For more information on liabilities, see Note 24 from page 246 onward

For more information on the Statement of Cash Flows, see the Management's Report from page 55 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 ensure solvency, limit financial risks and optimize the cost of capital.

Capital structure management focuses on meeting the requirements needed to ensure unrestricted access to the capital market and a solid "A" rating. The 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 €36,109 million as of December 31, 2018 (December 31, 2017: €34,756 million); the equity ratio was 41.7% on December 31, 2018 (December 31, 2017: 44.1%).

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.

BASF currently has the following ratings, which were most recently confirmed by Moody's on February 15, 2019, by Standard & Poor's on January 11, 2019, and by Scope Ratings on December 11, 2018.

Ratings as of December 31, 2018

	Noncurrent financial indebtedness	Current financial indebtedness	Outlook
Moody's	A1	P-1	stable
Standard & Poor's	A	A-1	stable
Scope	A	S-1	stable

Ratings as of December 31, 2017

	Noncurrent financial indebtedness	Current financial indebtedness	Outlook
Moody's	A1	P-1	stable
Standard & Poor's	A	A-1	stable
Scope	A	S-1	stable

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

For more information on BASF's financing policy, see the Management's Report from page 54 onward

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

Share price-based compensation program

The BASF Group continued its share price-based compensation program (the long-term incentive (LTI) program) in 2018. The program has been in place since 1999 and approximately 1,200 people, in particular the Board of Executive Directors and senior executives, are currently eligible to participate. It 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 trading day after the Annual Shareholders' Meeting, which was €85.45 on May 7, 2018.

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 on the option grant date (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 by which the BASF share outperforms the MSCI Chemicals Index on the exercise date. It is limited to the closing

price on the date of exercise less the nominal value of the BASF share. From the 2013 LTI program onward, right B may only be exercised if the price of the BASF share equals at least the base price. The options of the 2018 LTI program were granted as of July 1, 2018, and may be exercised following a two-year vesting period, between July 1, 2020, and June 30, 2026. 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 thresholds must be exceeded. If the other threshold is not exceeded 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 the BASF Group 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 four years after they have been granted at the earliest (vesting period).

The 2011 to 2017 programs were structured in a similar way to the 2018 LTI program.

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, 2018

		LTI program of the year	
		2018	2017
Fair value	€	10.5	6.25
Dividend yield	%	5.3	5.3
Risk-free interest rate	%	0.00	(0.12)
Volatility BASF share	%	25.32	23.22
Volatility MSCI Chemicals	%	15.97	14.14
Correlation BASF share price : MSCI Chemicals	%	78.27	75.24

The stated fair values and the valuation parameters relate to the 2018 and 2017 LTI programs. 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 and valuation parameters were determined/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 2,010,720 in 2018 (2017: 1,461,113).

As a result of a resolution by the Board of Executive Directors in 2002 to settle option rights in cash, all outstanding option rights under the 2011 to 2018 LTI programs were valued at fair value as of December 31, 2018. A proportionate provision is recognized for programs in the vesting period. The LTI provision decreased from €347 million as of December 31, 2017, to €56 million as of December 31, 2018, due to lower fair values of the outstanding option rights. The utilization of provisions amounted to €22 million in 2018 (2017: €49 million). Income arising from the release of provisions amounted to €268 million in 2018 (2017: €68 million). Of this

amount, €6 million was attributable to the disposal group for the discontinued oil and gas business in 2018 (2017: €1 million).

The exercisable options had no intrinsic value as of December 31, 2018; their total intrinsic value as of December 31, 2017 was €145 million.

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 permitted.

Employees who participate in BASF's “plus” incentive share program 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 these 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 a Group 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	2018	2017
As of January 1	2,811,447	2,849,723
Newly acquired entitlements	693,125	570,465
Bonus shares issued	(477,395)	(479,111)
Lapsed entitlements	(99,334)	(129,630)
As of December 31	2,927,843	2,811,447

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 BASF share price, 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 €85.45 for the 2018 program, and €86.02 for the 2017 program.

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

Personnel expenses of €32 million were recorded in 2018 for BASF's “plus” incentive share program (2017: €28 million).

31 Compensation of the Board of Executive Directors and Supervisory Board

Compensation of the Board of Executive Directors and Supervisory Board

Million €

	2018	2017
Non-performance-related and performance-related cash compensation of the Board of Executive Directors	14.3	24.8
Fair value of options granted to the Board of Executive Directors in the fiscal year as of grant date	4.5	2.7
Total compensation of the Board of Executive Directors	18.8	27.5
Service costs for members of the Board of Executive Directors	6.3	7.0
Compensation of the Supervisory Board	3.3	3.3
Total compensation of former members of the Board of Executive Directors and their surviving dependents ^{1,2}	(4.4)	7.6
Pension provisions for former members of the Board of Executive Directors and their surviving dependents	159.5	144.3
Guarantees assumed for members of the Board of Executive Directors and the Supervisory Board	–	–

¹ Total compensation of former members of the Board of Executive Directors includes compensation for Dr. Kurt Bock before pension benefits in the amount of approximately €1.1 million.

² Compensation for Dr. Harald Schwager and Margret Suckale for their active membership on the Board of Executive Directors in 2017 is included under total compensation of former members of the Board of Executive Directors in the amount of approximately €1.0 million each.

The annual variable compensation in effect until the end of 2017 was replaced as of 2018 with a forward-looking performance bonus that is geared to sustainable corporate development and has a three-year deferral component. The performance bonus is based on the performance of the Board of Executive Directors as a whole and the return on capital employed (ROCE) of the BASF Group. Subject to certain conditions, ROCE is adjusted for special items from acquisitions and divestitures. The conditions for the adjustment of ROCE were not met in 2018.

Until December 31, 2017, performance-related compensation of the Board of Executive Directors was based on the return on assets adjusted for special effects, as well as the performance of the Board of Executive Directors as a whole. Return on assets corresponds to income before income taxes plus interest expenses as a percentage of average assets.

The members of the Board of Executive Directors were granted 210,228 option rights under the long-term incentive (LTI) program in 2018. The market valuation of the option rights of active and former members of the Board of Executive Directors resulted in income totaling €28.5 million in 2018 (2017: €5.8 million).

For more information on the compensation of members of the Board of Executive Directors, see the Compensation Report from page 146 onward

For more information on the members of the Supervisory Board and Board of Executive Directors, including their memberships on other boards, see page 142 onward

32 Related party transactions

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

The following tables show the volume of business with related parties that are included in the Consolidated Financial Statements at amortized cost or accounted for using the equity method. The values include sales, receivables, other receivables, liabilities and other liabilities with respect to the disposal groups and/or discontinued operations.

Since the transfer of the leather chemicals business to the Stahl group as of September 29, 2017, BASF holds a minority interest in the parent company of the Stahl group, over which it can exercise significant influence. Sales, trade accounts receivable and other liabilities resulting from transactions with the Stahl group since then are included in the tables below in the values for associated companies for 2018 and 2017.

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 businesses.

Sales from joint ventures with BASF Group companies amounted to €543 million in 2018, and €598 million in 2017. Sales from associated companies with companies in the BASF Group amounted to €626 million in 2018, and €481 million in 2017.

Sales to related parties

Million €

	2018	2017
Nonconsolidated subsidiaries	530	413
Joint ventures	583	379
Associated companies	380	307

Trade accounts receivable from/trade accounts payable to related parties

Million €

	Accounts receivable, trade		Accounts payable, trade	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
Nonconsolidated subsidiaries	175	136	101	77
Joint ventures	91	69	75	75
Associated companies	78	71	42	29

Other receivables from/liabilities to related parties

Million €

	Other receivables		Other liabilities	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
Nonconsolidated subsidiaries	247	172	190	180
Joint ventures	284	306	432	734
Associated companies	70	73	271	236

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.

Both the increase in other receivables from nonconsolidated subsidiaries and the decrease in other liabilities to joint ventures in 2018 were due mainly to other finance-related receivables and/or liabilities.

The outstanding balances toward related parties were generally not secured and settled in cash.

The balance of valuation allowances for other receivables from nonconsolidated subsidiaries increased from €74 million as of December 31, 2017 to €76 million as of December 31, 2018. Of this amount, €2 million was recognized as an expense in 2018 (2017: €1 million).

The balance of valuation allowances for trade accounts receivable from associated companies decreased from €9 million as of December 31, 2017 to €8 million as of December 31, 2018.

There were obligations from guarantees and other financial obligations at BASF in favor of nonconsolidated subsidiaries in the amount of €6 million as of December 31, 2018 (December 31, 2017: €5 million), and in favor of associated companies in the amount of €17 million as of December 31, 2018 (December 31, 2017: €23 million).

Obligations arising from purchase contracts with joint ventures amounted to €3 million as of December 31, 2018 and €3 million as of December 31, 2017.

As of December 31, 2018, the present value of the outstanding minimum rental payments for an office building including a parking area payable by BASF SE to BASF Pensionskasse VVaG for the nonterminable basic rental period to 2029 amounted to €52 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 2018.

 For more information on subsidiaries, joint ventures and associated companies, see the BASF Group list of shares held on page 211

For more information on other financial obligations in favor of joint ventures, see Note 25 from page 249 onward

For more information about defined benefit plants, the division of risk between Group companies, see Provisions for pensions and similar obligations, from page 240 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 142 onward

33 Services provided by the external auditor

BASF Group companies used the following services from KPMG:

Services provided by the external auditor

Million €

	2018	2017
Annual audit	21.1	18.6
of which domestic	8.2	6.4
Audit-related services	0.7	0.4
of which domestic	0.5	0.1
Tax consultation services	0.3	0.2
of which domestic	0.1	0.1
Other services	–	0.1
of which domestic	–	–
Total	22.1	19.3

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 relates to expenses for the audit of the Consolidated Financial Statements of the BASF Group, the legally required financial statements of BASF SE and of the subsidiaries and joint operations included in the Consolidated Financial Statements as well as the voluntary audit of subgroups and combined financial statements. Tax consultation services refer primarily to fees for completion of unfinished tax returns. Fees for other services primarily include 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 of the German Stock Corporation Act (AktG)

The annual Declaration of Conformity with the German Corporate Governance Code according to section 161 AktG was signed by the Board of Executive Directors and the Supervisory Board of BASF SE in December 2018 and is published online.

🔗 For more information, see basf.com/en/corporategovernance

35 Non-adjusting post-balance sheet date events

On January 31, 2019, BASF and Solenis concluded the transfer of BASF's paper and water chemicals business to Solenis that had been announced in May 2018. BASF gained a share of 49% in Solenis as of February 1, 2019. 51% of the shares will be held by funds managed by Clayton, Dubilier & Rice and senior management. The transaction covered production facilities and plants pertaining to BASF's paper and water chemicals business in Bradford and Grimsby, United Kingdom, Suffolk, Virginia, Altamira, Mexico, Ankleshwar, India and Kwinana, Australia. The BASF Paper and Water Chemicals business unit's production plants that are tightly integrated in the Verbund in Ludwigshafen, Germany, and in Nanjing, China, will remain with BASF, supplying the joint company with products and raw materials based on medium and long-term supply agreements. BASF's paper coating chemicals portfolio was not part of the transaction. As of the closing of the transaction, BASF's share of Solenis' income after taxes will be accounted for using the equity method due to BASF's significant influence, and included in EBIT of the BASF Group, presented in Other.