

Abridged version of the Annual Report 2016

REPORT OF THE SUPERVISORY BOARD

for the financial year of RHÖN-KLINIKUM AG
from 1 January 2016 to 31 December 2016



Eugen Münch
Chairman of the Supervisory
Board

Dear Shareholders,
Dear Ladies and Gentlemen,

From the very beginning, the development of RHÖN-KLINIKUM AG has been characterised by continuity and change. The Company at all times has stood for excellent, progressive and at the same time affordable healthcare delivery in the best interests of our patients. When confronted with major entrepreneurial challenges, the Company has always been able to rely on its know-how and its strength. That is something that will also stand RHÖN-KLINIKUM AG in good stead right now as it embraces the impending changes and its strategic reorientation.

Digitalisation, and with it the greater use of powerful IT systems for diagnosis and therapy, will be a key component of the strategy in future. At the same time, though, digitalisation must not be an end in itself. Like all other technological and scientific developments of the past, it must serve the benefit of patients. The Management of RHÖN-KLINIKUM AG are therefore called upon to weigh up the opportunities and challenges of digitalisation against our ethical principles in a responsible and faithful manner.

As in the past, the Supervisory Board will escort this task critically and constructively in keeping with its statutory mandate.

COOPERATION BETWEEN SUPERVISORY BOARD AND BOARD OF MANAGEMENT

During financial year 2016 also, the Supervisory Board examined on an ongoing basis and in detail the situation and development of the Company, duly performing the duties incumbent on it by law, the Articles of Association and the Terms of Reference: these include continuously monitoring management activity and regularly advising the Board of Management in connection with the directing of the Company. At the same time the Supervisory Board, in performing its duties, was at all times guided by the decisive principles of appropriateness, compliance with legal provisions, expediency and efficiency. Observance of these principles by the Board of Management was monitored by regularly reviewing the Company's general organisation and verifying the instruments used for internal risk control.

The Supervisory Board was involved in fundamental and important decisions taken by the Board of Management of RHÖN-KLINIKUM AG. The Board of Management as a general rule complied with its information duties, keeping us informed on a timely basis both in written form and orally, with documents and records of relevance for decisions being provided to the Supervisory Board in good time prior to the respective deliberations and formal meetings. The Supervisory Board reviewed the reporting and the information submitted by the Board of Management regarding strategic and operative business performance, compliance issues as well as risks and risk management for plausibility and comprehensibility, discussed this with the Board of Management and also scrutinised the same whenever appropriate.

The areas of focus of deliberations with the corporate bodies and with the Board of Management were the further strategic development of the Group, issues, projects and measures aimed at re-orienting business activity towards the areas of cutting-edge medicine and university medicine as well as the activity of a full-service healthcare provider. The role of escorting the Board of Management in this process of change in an ongoing advisory capacity, e. g. in the implementation of the campus projects at the Bad Neustadt and Marburg sites, in the introduction of the electronic patient file or in the use of the cognitive computer system IBM Watson for anamnesis and diagnosis were among the key tasks of the Supervisory Board during the past financial year.

The chairman of the Supervisory Board moreover engaged in an intensive and regular exchange of information and ideas with the chairman of the Board of Management – also between meetings held by the corporate bodies – and was kept thoroughly informed at all times about material developments and current business transactions. The Board of Management complied with its duties to inform. We thoroughly discussed the resolution proposals made by the Board of Management and, to the extent required by statute, the Articles of Association and the Terms of Reference, voted on the same after a thoroughgoing review in the Supervisory Board and the respective competent Supervisory Board committees. In a few cases, we were advised and assisted by external experts and advisers in the interests of the shareholders. Where required in the case of particularly pressing and time-critical business matters, the Supervisory Board, or, as the case may be, the competent committee held meetings by means of conference calls and also adopted resolutions by voting in written form.

WORK OF THE SUPERVISORY BOARD IN COMMITTEES AND PLENARY MEETING

With a view to performing its tasks and assuming its responsibility in the best possible way, the Supervisory Board has set up a total of seven standing committees whose members possess specific expertise and experience for the special issues dealt within the committees. With regard to the key strategic issues of business policy, joint meetings of the Investment, Strategy and Finance Committee and of the Medical Innovation and Quality Committee with the Board of Management were held with further senior executives from the Group and the respective specialist fields being consulted. These meetings were also attended by representatives of the local works council from the respective Group sites.

The committees act as bodies with power to pass resolutions within the scope prescribed by law, the Articles of Association – also in lieu of the Supervisory Board – and the Terms of Reference of the latter to the extent consistent with statute and previously defined by the Supervisory Board. The committees generally meet separately from plenary meetings. Meetings were also held as conference calls convened on short notice as required.

The **Investment, Strategy and Finance Committee** held three ordinary meetings during the year under review (attendance rate: 100 per cent). A further three meetings (attendance rate 97 per cent) were held as joint meetings with the **Medical Innovation and Quality Committee**.

The areas focused on in the strategic discussions held at the joint meetings essentially covered the implementation of the Bad Neustadt campus project, the development of a university campus model for the Marburg site and – as already in the two previous years – the further development and implementation of network medicine using the electronic patient file and further applications from the field of IT/eHealth, such as the cognitive computer system Watson in anamnesis and diagnosis in cooperation with IBM. For the pilot project Bad Neustadt Campus the combined Committee, after careful deliberation, approved an investment framework for the construction measure of €235 million. For the Marburg university site, the Board of Management submitted a basic concept for construction of an outpatient and diagnosis centre, a centre for mental health (psychiatry and psychosomatics) and further construction measures whose conceptional and planning preparation was approved by the Committee. Investment approval and thus the project's realisation are to take place only when the business management basis has been established through a change in the procedure in the separate accounting approach resulting in appropriate cost reimbursement by the Federal State of Hesse for research and teaching.

At the ordinary meetings of the Investment, Strategy and Finance Committee, the chairman of the Board of Management reported on current developments in the industry and on the business position of the Group, as well as on the development of investments and financing in a continuously updated investment and finance plan. Specific motions for approval of investment projects and financing measures were subsequently openly discussed, critically reviewed and – after the members carefully considered and were fully convinced of the same – adopted in the Committee based on detailed written resolution proposals of the Board of Management, including market studies and investment calculations. In a regular acquisition report, the Board of Management provided an overview of the national hospital market which served as the basis of discussion for planned and ongoing acquisition projects.

The focus of interest of the supervision and deliberations at all meetings was the economic development of the subsidiary Universitätsklinikum Gießen und Marburg GmbH (UKGM), in particular the efforts and negotiations with the Federal State of Hesse to achieve an appropriate cost reimbursement of expenditure for research and teaching by improving the terms of the separate accounting approach. Measures to increase the number of patient treatments at the Marburg Particle Centre were just as much a focus of interest as the planned measures to improve the workload of staff resulting from the evaluation of an employee survey at UKGM.

The Committee approved the establishment of RHÖN-Innovations GmbH, an investment company whose objective is to fund innovative start-ups, and kept itself regularly informed about its continued development. Further issues were rationalisation measures in the area of materials management, raising the quality of medical care, and the effects that might arise from the change from the MDAX® exchange segment to the SDAX®.

During the reporting year, the **Personnel Affairs Committee** held one physical meeting and one conference call (attendance rate in each case: 100 per cent).

The group of participants of the physical meeting was enlarged in each case by a member of the shareholder and employee representatives exclusively for such meeting.

The Committee dealt with the appraisal and evaluation of the performance and development of the individual members of the Board of Management and of the Board of Management as a whole. At the same time, both the expectations of the members of the Board of Management as well as their prospects and expectations regarding the Company's development in the medium term were discussed. The Committee prepared personnel decisions of the Supervisory Board and, with a view to strengthening and reorganising the Company's management, after conscientious and careful consideration, submitted resolution proposals to the Supervisory Board on the appointment of a new chairman of the Board of Management, on amendments to the Terms of Reference of the Board of Management, and on the conclusion of a Board of Management service contract.

During the past financial year, the **Mediation Committee** (pursuant to section 27 (3) of the Co-Determination Act (Mitbestimmungsgesetz, MitBestG)) also did not have to be convened.

The **Audit Committee** of the Supervisory Board met five times in the year under review (attendance rate: 90 per cent). All meetings were attended by the Board of Management. Two meetings were attended by the statutory auditor, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft (PwC). For selected agenda items, the heads of the Internal Auditing, Compliance as well as Accounting, Tax and Controlling departments were regularly consulted by the Board of Management, and were available to the Committee for additional reports and questions.

This Committee notably was responsible for reviewing and preparing the RHÖN-KLINIKUM AG consolidated annual financial statements for financial year 2015. Also reviewed and discussed were the stand-alone financial statements, the management reports and the respective audit reports of the Group subsidiaries which were subjected to critical review by the members of the Committee, as well as the proposal on the appropriation of the net distributable profit.

The Audit Committee assessed the independence of the auditor designated for auditing the annual financial statements for financial year 2016 and for the review of the Half-Year Financial Report, obtained the statement regarding the auditor's independence pursuant to Item 7.2.1 of the German Corporate Governance Code, recommended to the plenary meeting of the Supervisory Board a proposal for the election of the auditor to be submitted to the Annual General Meeting and – after the election – issued the auditor with the audit mandate and concluded with him a reasonable remuneration agreement for the same. The statutory auditor moreover reported to the Committee on orders for services performed in addition to the auditing services rendered. The qualification of the statutory auditor was monitored by the Committee. A list of audit items was once again developed and defined for the audit in 2016.

Questions of fundamental importance relating to accounting, corporate planning, the capital base, the supervision of the accounting process, as well as the effectiveness of the internal controlling system, risk management system (including special business risks), and the internal audit system were discussed with the Board of Management and in some cases also with the statutory auditor. The interim reports were thoroughly discussed on a regular basis with the Board of Management prior to their publication, as well as the half-year financial report with the Board of Management and in the presence of the statutory auditor giving due regard to the review by the latter.

The Group controlling report on performance and finance controlling submitted quarterly, which forms part of our risk management system, was thoroughly discussed at every meeting with the Board of Management. Here, the development of service volumes and earnings of the Group and of the individual Group hospitals was also analysed, questioned and discussed with the Board of Management, also with regard to deviations from targets.

The body kept itself regularly informed about the activity of the Internal Auditing department by the responsible member of the Board of Management and by reports submitted by the head of Internal Auditing, and examined the auditing plan for 2016 as well as its update. The audit reports of the Internal Auditing department as well as the 2015 activity report were then submitted and discussed with the Board of Management. We kept ourselves informed by the Board of Management on the implementation of the recommendations by the Internal Auditing department through information on the results of follow-up reporting and inspection. We once again satisfied ourselves of the effectiveness of the Internal Auditing department.

In three meetings, the members of the Committee examined the current developments in legislation and accounting arising from the EU Audit Reform and the implementation of the German Act Reforming the Audit of Annual Financial Statements (Abschlussprüfungsreformgesetz, AReG). They had themselves informed by PwC on the new provisions for the Audit Committee, on the reports by the statutory auditor and on the approach and quality assurance in the context of the audit of the annual accounts and well as on the development of a list for advance approval of non-auditing services of the statutory auditor and the budget for provision of non-auditing services.

In updating the Declaration of Compliance pursuant to section 161 of the German Stock Corporation Act (Aktiengesetz, AktG) relating to the recommendations of the German Corporate Governance Code, the version of 5 May 2015 was reviewed as to its application and duly reflected, with a corresponding resolution proposal being submitted to the Supervisory Board as a whole.

The **Committee for Compliance and Communication** serves to advise and supervise the Board of Management and senior executives with respect to compliance with legal and other provisions as well as with regard to communication by the Company with the media and the capital market. To ensure close and non-bureaucratic coordination with the Audit Committee, which among other things is responsible for supervising the Internal Auditing department, the chairman of the Committee for Compliance and Communication is assigned a seat on the Audit Committee.

In 2016, the Committee met five times (attendance rate: 85 per cent). The Board of Management was represented at all meetings and was assisted in the deliberations by the Central Compliance and Internal Auditing departments as well as the heads of the Group divisions of Corporate Communications and Investor Relations.

The focus of interest of the meetings was the ongoing compliance reports from headquarters and the individual sites, the design and Company-wide introduction of the eLearning programme for enhancing efficiency and quality, and the further improvement of cooperation on compliance matters between Group headquarters and the compliance officers of the individual sites. In the area of corporate communications, the Board of Management reported on the Company's communications strategy and various projects. The equity story and the perception of the Company, above all with analysts and institutional investors, as well as the causes and impact of the change in segment from the MDAX® to the SDAX®, were the key focus of the discussions on capital market issues.

The **Medical Innovation and Quality Committee** provides the Board of Management with technical advice on developments and trends in medicine and monitors the situation and development of medical quality within the Company. During the reporting year, the Committee did not hold any separate meetings but convened exclusively in three joint meetings with the Investment, Strategy and Finance Committee (see above).

The **Nomination Committee**, which selects candidates from the shareholders' representatives for supervisory board office and proposes them to the Supervisory Board, did not have to be convened during the financial year.

During the reporting year, four regular meetings of the full Supervisory Board were held (attendance rate: 94 per cent). No member of the Supervisory Board attended fewer than half the meetings of the Supervisory Board and the Committees attached to it. The members of the Board of Management attended the meetings of the Supervisory Board except in the case of agenda items relating to internal matters of the Supervisory Board and matters pertaining to the Board of Management.

At the four ordinary meetings of the **Supervisory Board** the plenary meeting, based on detailed reports of the chairman of the Board of Management on current developments and the business position of the Group, the written reports and presentations by the Board of Management, regularly deliberated together with the Board of Management on the net assets, financial position and results of operations, the trend in revenues and earnings, the performance data, key figures and personnel of the Company and Group as well as of the individual Group subsidiaries. The respective interim reports for the past quarters were explained by the Board of Management in detail at the plenary meeting prior to publication.

At the first meeting of the financial year on 25 February 2016, the Supervisory Board first of all examined issues of remuneration for adjusting the management profit sharing bonuses of the Board of Management for 2015 and adopted the corresponding resolution after a thoroughgoing discussion. On the recommendation of the Investment, Strategy and Finance Committee, and after intense discussion, approval was given to the establishment of the investment company RHÖN-Innovations GmbH in which a limited equity participation of the Management is permitted. To escort the Group's development concepts – Bad Neustadt and Marburg campus projects, concept for computer-assisted anamneses and diagnosis, network with medical-related content –, resolutions with a view to reorganising the committee work of the Supervisory Board were adopted to dissolve the existing Network Medicine working group and on the possibility of combined meetings of the Investment, Strategy and Finance Committee with the Medical Innovation and Quality Committee. We received the report of the Board of Management on the preliminary 2015 annual financial statements and approved the submitted drafts of the Report of the Supervisory Board and the Corporate Governance Report for financial year 2015.

At the balance sheet meeting on 14 April 2016 also attended by the statutory auditors, the plenary meeting discussed the annual financial statements and management report of RHÖN-KLINIKUM AG as well as the consolidated financial statements and the Group management report for financial year 2015 together with the Board of Management and the statutory auditor PwC. The auditors reported on the essential findings and results of the audits and were available to the Supervisory Board for questions and additional information. The plenary meeting approved the annual financial statements. Also discussed at this meeting were the preparations for the Annual General Meeting on 8 June 2016, in particular the adoption of resolution recommendations of the Supervisory Board on the resolution proposals in the agenda items for the Annual General Meeting after a prior discussion of the agenda items. Further approval resolutions were adopted for the Report of the Supervisory Board, Corporate Governance Report and the Declaration on Corporate Governance pursuant to section 289a of the German Commercial Code (Handelsgesetzbuch, HGB). In exercise of the equity participation rights of RHÖN-KLINIKUM AG with regard to Universitätsklinikum Gießen und Marburg GmbH (UKGM), resolutions were adopted regarding the appointment of the Supervisory Board. Furthermore, with regard to UKGM the issues of the outpatient and diagnosis centre, separate accounting and the result of an employee survey (COPSOQ survey) on employee satisfaction were discussed.

At the meeting on 6 July 2016, the plenary meeting was thoroughly informed about the results of the consultations and the resolutions of the preceding two-day joint meeting of the Investment, Strategy and Finance Committee with the Medical Innovation and Quality Committee on the campus projects and applications from the field of IT/eHealth. Other areas of focus of the deliberations were the development of patient numbers at the Marburg Particle Therapy Centre, business performance and earnings targets for the Group's facilities as well as a progress report on the development of the investment company RHÖN-Innovations GmbH.

At the Supervisory Board Meeting on 3 November 2016, the plenary meeting first decided to consult once again an external expert to conduct an efficiency audit regarding the activity of the Supervisory Board. After a detailed discussion on the determination of the assessment basis for calculating the management profit sharing bonuses for 2016, the key elements were defined. The subject matter of extensive reporting by the Board of Management, besides the usual Management Report and Annual Report and the reports by the individual facilities, also covered the issues of internal Group communication, the development and implementation of the RKA Quality Cockpit (an internal Group medical reporting scheme) and a status report on materials management. The resolution recommendation by the Audit Committee on the annually submitted Declaration of Compliance pursuant to section 161 of the German Stock Corporation Act (Aktiengesetz, AktG) regarding the recommendations of the German Corporate Governance Code was approved.

CORPORATE GOVERNANCE CODE AND DECLARATION OF COMPLIANCE

During the past financial year, the Supervisory Board also examined the further development and implementation of the recommendations and suggestions as set out in the German Corporate Governance Code. The Declaration of Compliance issued on 5 November 2015 pursuant to section 161 of the Stock Corporation Act (Aktiengesetz, AktG) was revised and, giving due regard to the Code as amended on 5 May 2015, was replaced by an updated Declaration of Compliance issued on 3 November 2016 by the Board of Management and the Supervisory Board. The declarations were permanently made available to the shareholders on the Company's website. In accordance with Item 3.10 of the German Corporate Governance Code, the Board of Management and the Supervisory Board jointly report on corporate governance from page 25 of this Annual Report.

EXAMINATION AND APPROVAL OF THE 2016 FINANCIAL STATEMENTS

The Board of Management adopted the financial statements of the Company and the management report for the year ended 31 December 2016 in accordance with the provisions of the German Commercial Code (HGB), while the consolidated financial statements and Group management report for the year ended 31 December 2016 were adopted pursuant to section 315a of the German Commercial Code (HGB) in accordance with the principles set out in the International Financial Reporting Standards (IFRS). The auditors, PricewaterhouseCoopers Deutsche Revision Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Frankfurt am Main, have examined the financial statements of the Company and Management's report as well as the consolidated financial statements and Management's consolidated report for the year ended 31 December 2016. The auditors of the accounts issued an unqualified auditor's report in each case.

The financial statements of the Company and management report, the consolidated financial statements and Group management report as well as the reports of the auditors on the result of their audit were received by all members of the Supervisory Board together with the Management's proposal for the appropriation of the net distributable profit for the year. These documents were examined by the Supervisory Board and extensively discussed by the Audit Committee and by the Supervisory Board with representatives of the auditors at the respective balance sheet meetings. As part of the audit, the Audit Committee and the Supervisory Board examined both the accounting findings and the procedures and processes relating to the accounting findings. As the standard of their review, they primarily applied the criterion of legality and verified whether the documents submitted comply with legislation in force and in particular with applicable accounting rules. Furthermore, in addition to their review of legality they also conducted an expediency review in terms of accounting, financial and business policy aspects. Based on the findings of the preliminary review by the Audit Committee, the Supervisory Board concurred with the findings of the auditors and, having conducted its own review, determined that it sees no grounds for objections.

The Supervisory Board approved the financial statements of the Company and the consolidated financial statements prepared by the Board of Management at the meeting on 6 April 2017 on recommendation of the Audit Committee; the financial statements of the Company are thus adopted as final.

The Supervisory Board approves the Board of Management's proposals for the appropriation of net distributable profit.

CHANGES AND COMPOSITION OF THE BOARD OF MANAGEMENT

This Annual Report presents the composition of the Board of Management and the personal data, functions and duties of the individual members of the Board of Management under the heading "Corporate bodies of the Company".

Prof. Dr. Bernd Griewing was appointed with effect from 1 January 2016 as member of the Board of Management for the term of five years. As chief medical officer (CMO), he assumed responsibility for the newly created corporate division Medical. The appointments of the other members of the Board of Management were in each case harmonised re-appointment as of 1 January 2016 for a further term of five years in each case.

With effect from 1 February 2017, Mr. Stephan Holzinger was appointed as a new member of the Board of Management for five years and was appointed as chairman of the Board of Management. The previous chairman of the Board of Management, Dr. Dr. Martin Siebert, assumed the office of permanent representative of the chairman of the Board of Management. At its meeting on 23 February 2017, the Supervisory Board resolved to reduce the number of the members of the Board of Management to the number provided for in the Articles of Association (three). The members of the Board of Management Martin Menger and Jens-Peter Neumann were removed at this meeting.

CHANGES AND COMPOSITION OF THE SUPERVISORY BOARD

In accordance with the requirements of the Co-Determination Act (MitBestG) and after the effective date of the amendment of the Articles of Association in § 10 (Size and composition of Supervisory Board) adopted by the 2014 Annual General Meeting, the Supervisory Board of RHÖN-KLINIKUM AG as of 10 June 2015 is comprised of 16 members. Eight Supervisory Board members were elected by the shareholders and eight Supervisory Board members by the employees.

No changes in personal details occurred during the year under review. Mr. Stephan Holzinger resigned his Supervisory Board mandate with effect from 31 January 2017 after being appointed as member of the Board of Management. The Nomination Committee nominated Dr. Annette Beller, member of the management board of B. Braun Melsungen AG, to succeed on the Supervisory Board. Upon announcement of the decision by the Local Court of Schweinfurt of 22 March 2017, Dr. Annette Beller was appointed as a member of the Supervisory Board until the next Annual General Meeting on 7 June 2017.

The personal details of the members of the Supervisory Board in 2016 are set out in the Notes to the consolidated financial statements. The section also provides information on the professional qualifications of the Supervisory Board members as well as their further mandates. The organisational structure of the Supervisory Board and the composition of the committees during the past financial year are set out in the overview provided following this Report.

The Supervisory Board thanks the members of the Board of Management, all employees of the Group as well as the employee representatives of all Group companies for their commitment and work performed during the past financial year.

Bad Neustadt a. d. Saale, 6 April 2017

The Supervisory Board

Eugen Münch
Chairman

OVERVIEW OF THE ORGANISATIONAL STRUCTURE OF THE SUPERVISORY BOARD AND COMPOSITION OF THE STANDING COMMITTEES

(period of 1 January–31 December 2016)

CHAIR OF THE SUPERVISORY BOARD

Chairman
Eugen Münch

1st deputy Chairman
Georg Schulze-Ziehaus

2nd deputy Chairman
Wolfgang Mündel

COMPOSITION OF THE COMMITTEES

INVESTMENT, STRATEGY AND FINANCE COMMITTEE

Eugen Münch
Chairman
Björn Borgmann
Prof. Dr. Ludwig Georg Braun
Stefan Härtel
Klaus Hanschur
Stephan Holzinger
Wolfgang Mündel
Georg Schulze-Ziehaus

PERSONNEL AFFAIRS COMMITTEE

Eugen Münch
Chairman
Stefan Härtel
Dr. Brigitte Mohn
Georg Schulze-Ziehaus

MEDIATION COMMITTEE

Eugen Münch
Chairman
Prof. Dr. Ludwig Georg Braun
Meike Jäger
Georg Schulze-Ziehaus

AUDIT COMMITTEE

Wolfgang Mündel
Chairman
Peter Berghöfer
Stephan Holzinger
Meike Jäger
Christine Reißner
Dr. Katrin Vernau

COMMITTEE FOR COMPLIANCE AND COMMUNICATION

Stephan Holzinger
Chairman
Bettina Böttcher
Evelin Schiebel
Dr. Katrin Vernau

MEDICAL INNOVATION AND QUALITY COMMITTEE

Eugen Münch
Chairman
Prof. Dr. Ludwig Georg Braun
Prof. Dr. Gerhard Ehninger
Klaus Hanschur
Evelin Schiebel

NOMINATION COMMITTEE

Eugen Münch
Chairman
Dr. Brigitte Mohn
Wolfgang Mündel