In its meeting on December 16, 2022, the Supervisory Board considered various compensation issues. It reviewed the Board of Management's fixed compensation on a regular basis and considered the long-term variable compensation for the Board of Management. The Board additionally discussed in detail the financial planning for fiscal 2023 proposed by the Board of Management and the medium-term outlook also presented. It approved both the financial plan and the financing framework proposed for fiscal 2023. In this meeting, the Supervisory Board also planned the AGM to be held in the year 2023, discussing the agenda and proposed resolutions and approved the decision of the Board of Management to hold the 2023 AGM as a virtual meeting. In this meeting, the Supervisory Board also voted to issue an unqualified declaration of conformity with the GCGC.

Covestro AG Supervisory Board (as of December 31, 2022; from left to right):
First row: Dr. Richard Pott, Petra Kronen, Dr. Christine Bortenlänger, Dr. Christoph Gürtler
Second row: Lise Kingo, Irena Küstner, Frank Löllgen, Petra Reinbold-Knape
Third row: Dr. Sven Schneider, Regine Stachelhaus, Marc Stothfang and Patrick Thomas

Committees of the Supervisory Board

In the past fiscal year, the Supervisory Board had five permanent committees set up so that it can continue to exercise its duties effectively and efficiently. The committees prepared resolutions by the full Supervisory Board and provided information on other topics to be discussed by this body. Moreover, certain decision-making powers of the Supervisory Board were delegated to the committees to the extent legally permissible. The Supervisory Board currently has the following permanent committees: Presidial Committee, Audit Committee, Human Resources Committee, Nominations Committee, and Sustainability Committee.

The tasks and responsibilities of the standing committees and their current composition are described in greater detail in “Declaration on Corporate Governance” under “Committees of the Supervisory Board” in the Combined Management Report.

The meetings and decisions of all committees, and especially those of the Audit and Sustainability Committees, were prepared on the basis of reports and explanations provided by the Board of Management. The committee chairs regularly provided comprehensive reports on the work of the committees to the full Supervisory Board.

The **Presidial Committee**, on which shareholders and employees are equally represented, made preparations in the year 2022 for the decisions relating to the qualification matrix required by the new GCGC and convened for a meeting for this purpose on November 23, 2022. This followed the preparation by the Nomination Committee of a proposed qualification matrix, including a review of and adjustments to the Supervisory Board's areas of skill.

The **Audit Committee** met a total of four times in the year under review: on February 21, May 2, July 25, and October 24, 2022, each time in the presence of the CFO. Three of these meetings were also attended by the auditor. The Audit Committee conducted a preparatory review of the Financial Statements of Covestro AG, the Consolidated Financial Statements of the Covestro Group, the Combined Management Report, and the proposal for the use of the distributable profit for the Supervisory Board. Additionally, it also discussed in detail the respective audit report and in particular, along with the oral report by the auditor on the material results of the audit. The Combined Management Report also included the Group's nonfinancial statement. In conducting its review, the Audit Committee found no grounds for objections. It recommended to the Supervisory Board to approve the Financial Statements and Consolidated Financial Statements for fiscal 2021 as well as to consent to the Combined Management Report and the proposal for the use of the distributable profit. In addition, the Audit Committee discussed with the Board of Management the half-year financial report in light of the results of the review by the auditor, and the Q1 and Q3 2022 interim statements prior to their publication.

The Audit Committee monitored the accounting and financial reporting process and the appropriateness and effectiveness of the internal control system, the risk management system, and the internal audit system, including sustainability-related aspects, and deliberated on the audit of the Financial Statements and compliance. In doing so, the Committee received reports, including from the heads of Corporate Audit and the Corporate Law, Intellectual Property & Compliance functions and from the auditor. No material weaknesses were identified in the internal control system for financial reporting purposes or the risk early warning system.

The Audit Committee additionally undertook preparations for the Supervisory Board's proposal for the appointment of the financial statement auditor by the AGM, the engagement of the auditor and agreement on the auditor's fee. It monitored the quality of the audit and the independence of the auditor as well as the supplementary non-audit services provided in addition to the financial statement audit. In this context, the committee had the auditor confirm their independence.

The Audit Committee discussed the audit risk assessment, audit strategy, audit planning, key audit matters, and audit results with the auditor. The Chairman of the Audit Committee had regular feedback sessions with the auditor on the audit progress and reported on this to the Audit Committee.

Particular topics discussed by the Audit Committee in the fiscal year under review were current and future regulatory requirements for sustainability reporting and their implementation, including especially the requirements of the EU Taxonomy; the amendments to the GCGC; pension plan asset management; information security; and cyber risk management. Furthermore, the Audit Committee obtained information on an ongoing basis on enhancements to the compliance management system (particularly regarding anti-corruption measures), the handling of suspected compliance violations, progress in significant litigation, new legal and regulatory risks, and the risk situation, risk tracking, and risk monitoring in the Group. The Corporate Audit function provided regular reports about risk assessments.

The heads of the relevant corporate functions also participated in meetings of the Audit Committee on selected agenda items, reported on these, and answered questions. In addition, the Chair of the Audit Committee discussed important matters between meetings, particularly with the Supervisory Board Chair, the CFO and the auditor. The key results of these discussions were reported regularly to the Audit Committee and the Supervisory Board. The Audit Committee continued its practice of closed sessions in the year under review. They allow the auditor and the committee during the meeting to have a discussion without the Board of Management being present.

In the reporting period, the **Human Resources Committee** met for a total of five meetings held on February 22, April 21, June 9, September 28, and December 16, 2022. Topics of particular importance in connection with long-term succession planning for the Board of Management in the past year also included the reappointment of the CEO, Dr. Markus Steilemann, and the extension of his contract as well as succession planning for the CTO. The CTO succession planning was on the agenda of the Human Resources Committee meetings in February, June, and September.

In its first meeting on February 22, the committee discussed the CTO succession planning, as well as target attainment by the members of the Board of Management, long-term variable compensation of the Board of Management, and adjustments to the description of the compensation system for the Board of Management. The meetings on April 21 and June 9 focused on the reappointment of the CEO and the extension of his contract.

In the fourth meeting held on September 28, the Human Resources Committee dealt in particular with the reappointment of Dr. Klaus Schäfer and the extension of his contract and the appointment of Dr. Thorsten Dreier as member of the Board of Management and successor to Dr. Schäfer as of July 1, 2023. It also approved Dr. Thomas Toepfer's membership of the Regional Advisory Council for the Central Region of Commerzbank AG.

The agenda of the meeting held on December 16 included the annual review of the appropriateness of Board of Management compensation, long-term variable compensation of the Board of Management, and short-term variable compensation for the current year.

The members of the **Nomination Committee** held a meeting on September 22 of the reporting year to discuss the skills profile and the qualification matrix of the Supervisory Board required by the GCGC. The Nomination Committee reviewed and added to the skills profile to meet the requirements of the new version of the GCGC. In this meeting, the Nomination Committee also prepared the qualification matrix required by the GCGC, which was subsequently processed further by the Presidial Committee.

The **Sustainability Committee** convened for a total of five meetings. In its first meeting on February 1, it dealt with Covestro's path to climate neutrality (Scope 1 and Scope 2 emissions) and related proposals on objectives and implementation measures. The committee also discussed the EU's chemicals strategy and the approach adopted by Covestro in response. In its second meeting on March 30, the focus was on Scope 3 emissions and how they relate to the circular economy. In the third meeting on June 7, the Scope 3/circular economy topic was raised again on the basis of examples from the market. In addition, discussions centered on ratings by external rating agencies on environmental, social, and governance (ESG) aspects, and the approach pursued by Covestro in this regard. Another topic at this meeting was the concept for the K plastics trade fair in October 2022, with a focus on sustainable solutions and the circular economy. In the fourth meeting on September 9, the committee discussed the key performance indicators (KPIs) for measuring performance against targets. It also considered the ESG aspect of "Compliance with human rights" and spent time on the topic of "Transparency of our reporting" (current forms of reporting at Covestro and future requirements, in particular in accordance with the EU Taxonomy Regulation and the Corporate Sustainability Reporting Directive). The topics focused on at the fifth meeting on November 25 included a progress update on ESG reporting, the 2022 materiality assessment, and the annual planning of the topics of the Sustainability Committee for the year 2023.

MANAGEMENT REPORT PROFILE

Combined Management Report of the Covestro Group and Covestro AG

The Combined Management Report pertains to both the Covestro Group and Covestro AG. This report covers the period from January 1 to December 31, 2022. The presentation of the results of operations, financial position, and net assets as well as the expected development, including the principal opportunities and risks, relate to the Covestro Group, unless otherwise noted. Information that applies to Covestro AG only is identified accordingly. The results of operations, financial position, and net assets of Covestro AG are presented in a separate chapter of the Report on Economic Position. In addition, the nonfinancial statement pursuant to Sections 315b and 315c in conjunction with Sections 289c through 289e of the HGB is integrated into the Group Management Report. This includes the statements in accordance with the European Union's Taxonomy Regulation (2020/852). A nonfinancial statement in accordance with Sections 289c through 289e of the HGB does not have to be provided for Covestro AG.

Nonfinancial Reporting

Covestro reports comprehensively and transparently about topics important from the company's perspective and for our stakeholders. We measure our sustainability performance using financial indicators as well as key nonfinancial indicators published in the Group Management Report. Our objective here is to highlight how closely linked environmental and societal factors are with responsible corporate governance and the long-term success of our business. The Group Management Report and the supplementary sustainability information together comprise our annual sustainability reporting. We supplement the nonfinancial information in the Group Management Report by reporting additional content, which meets the requirements of the "with reference to GRI" reporting option of the Global Reporting Initiative's (GRI) Sustainability Reporting Standards (SRS) and is identified separately.

For all reportable aspects, the nonfinancial statement includes the policies we pursue in addressing environmental matters, employee matters, and social matters as well as respect for human rights and anti-corruption and bribery matters, the due diligence processes followed, as well as the outcomes of these strategies. Nonfinancial performance indicators are reported only when these are important to the Covestro Group.

As an integral part of the Group Management Report, the nonfinancial statement was audited with reasonable assurance by our auditor, KPMG AG Wirtschaftsprüfungsgesellschaft, Düsseldorf (Germany). The supplementary sustainability information specifically identified as such additionally contributes to the transparency of our reporting, which meets the requirements of the "with reference to GRI" reporting option of the Global Reporting Initiative's (GRI) Sustainability Reporting Standards (SRS). We voluntarily report the management approaches for material topics in accordance with GRI 3-3 (2021). The supplementary sustainability information that is not part of our statutory audit of the Consolidated Financial Statements was subjected to a separate review with limited assurance pursuant to the International Standard on Assurance Engagements (ISAE) 3000 by KPMG AG Wirtschaftsprüfungsgesellschaft, Düsseldorf (Germany).

Environmental Performance Indicators

Environmental protection performance indicators are reported for all fully consolidated companies. Since these figures are calculated only at the end of the year, they include the group of companies consolidated as it stands at year-end. In this process, we incorporate data from all environmentally relevant Covestro sites, i.e., all production sites and relevant administrative sites. This data is used in addition to the environmental reporting contained in this report to communicate with various stakeholders, e.g., associations, the press, and government agencies, as well as to continually improve our environmental performance. In order to comply with publication deadlines, the sites estimate the environmental data for the final weeks of the current fiscal year on the basis of established estimation methodologies that ensure accurate reporting of data as close as possible to the actual figures for the year. If, however, in the course of the following year, we become aware of material deviations based on internally defined thresholds, the figures in question are corrected retroactively. This was not required in fiscal 2022 for the preceding fiscal year 2021.

The reporting of direct greenhouse gas (GHG) emissions, e.g., from burning fossil energy sources and from our production processes (Scope 1), of indirect GHG emissions from the provision and use of energy produced outside the company (Scope 2), and of GHG emissions from upstream and downstream processes in the value chain (Scope 3), is based on the requirements of the Greenhouse Gas Protocol and includes all fully consolidated companies. If, in our efforts to achieve climate neutrality, measures are taken to offset emissions in relation to our Scope 1 and Scope 2 GHG emissions, they are disclosed in accordance with the Greenhouse Gas Protocol. The global warming potential (GWP) factors correspond to the Fifth Assessment Report by the Intergovernmental Panel on Climate Change (IPCC).

Alternative Performance Measures

Throughout its financial reporting, Covestro uses alternative performance measures (APMs) to assess the business performance of the Group. These are not defined in the International Financial Reporting Standards (IFRSs) adopted by the European Union (EU). These non-IFRS indicators should be considered a supplement to, not a replacement for, the financial performance measures determined in accordance with IFRSs. The alternative performance measures of relevance to the Covestro Group include earnings before interest, taxes, depreciation, and amortization (EBITDA), return on capital employed (ROCE), free operating cash flow (FOCF), and net financial debt. The calculation methods for the APMs may vary from those of other companies, thus limiting the extent of the overall comparability. These alternative performance measures should not be viewed in isolation or employed as an alternative to the financial indicators determined in accordance with IFRSs and presented in the Consolidated Financial Statements for purposes of assessing Covestro's results of operations, financial position, and net assets.

→ **Explanations of the definition and calculation of these alternative performance measures can be found in the "Management" section.**

Internal Control System to Ensure Compliance

Compliance risks are systematically identified and assessed as part of Covestro's Group-wide risk management. Risk owners assess the compliance risks that have been identified. A risk matrix is used to define focal points of compliance tasks at Covestro. The findings of a risk-based analysis enabled Covestro to identify four key topics: antitrust law, corruption, data protection, and foreign trade law. The General Counsel/Chief Compliance Officer is the risk owner responsible for breaches of antitrust law and corruption, while the Global Export Control Officer oversees the risk of breaches of foreign trade law, and the Group Data Protection Officer is assigned to handling the risk of loss and improper handling of personal data. With respect to corruption, areas including gifts and invitations, relationships with government officials, and relationships with certain business partners such as sales agents were identified as being especially risk-relevant. A corruption risk analysis was performed in the year under review for all companies in which Covestro holds a majority interest. If the risk profile changes, new controls are implemented if needed.

Many controls have been implemented at both the global and local levels to reduce the number of compliance risks. To the extent possible, we integrate the compliance controls into our internal control system. The effectiveness of the compliance controls is evaluated on the basis of a cascaded self-assessment system, as are the ICS processes for accounting and financial reporting. The results of the effectiveness evaluations are documented in the global system for the ICS processes. The Corporate Audit function regularly reviews the compliance activities in independent, objective audits as part of dedicated compliance checks in the larger companies. In the smaller companies, compliance aspects are part of a general review.

Risk Management System

Covestro has implemented a structured risk management process for the early identification of any potentially disadvantageous developments that could have a material impact on our business or endanger the continued existence of the company. This process satisfies the legal requirements regarding an early warning system for risks pursuant to Section 91, Paragraph 2 of the German Stock Corporation Act, and is aligned with the international risk management standard COSO II Enterprise Risk Management – Integrated Framework (2004).

Risk management system

Corporate Risk Management defines, coordinates, and monitors the framework and standards for this risk management system, ensuring adequate risk communication and reporting to both management and the risk managers. Covestro uses risk management software that simplifies the aggregation of risks, provides displays of various interdependencies, and compares individual risks to the risk bearing capacity.

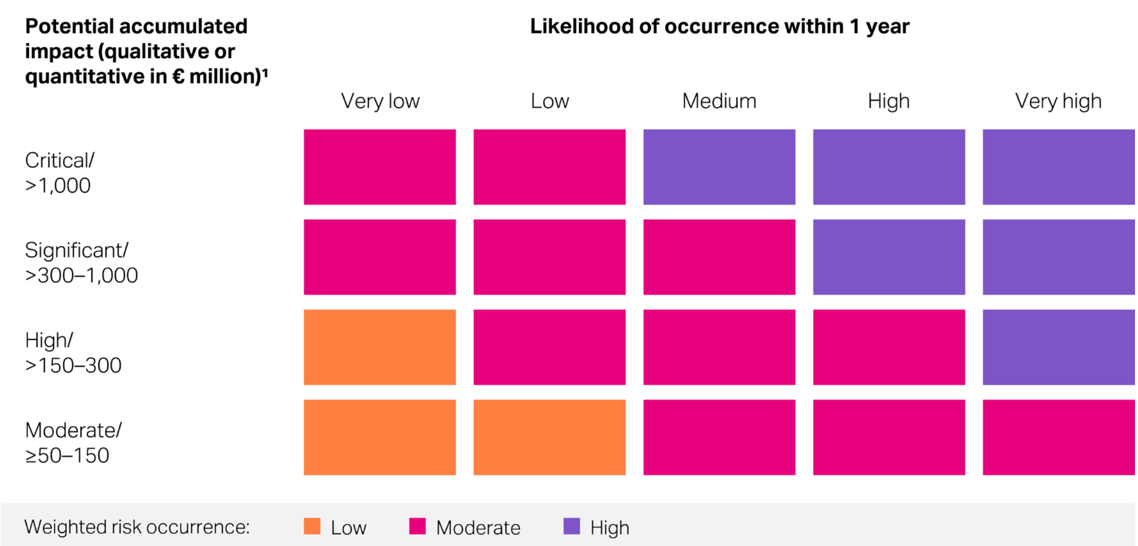
Risks are identified, evaluated, and controlled in the operating divisions and corporate functions by the respective risk managers, who are organized in various global sub-committees. The Covestro Corporate Risk Committee met three times in fiscal 2022 to review the risk landscape as well as the various risk management and monitoring mechanisms that are in place, and to take any necessary measures. Additionally, we conduct an ad-hoc process for newly identified risks throughout the year so that these are immediately incorporated into the risk management system. These ad-hoc risks are identified and their handling is determined based on risk assessments and depending on the defined thresholds. In addition, the Corporate Audit function complements the monitoring process with process-independent monitoring.

Financial risks are evaluated using estimates of the potential impact after taking into account countermeasures and the likelihood of their occurrence. The potential economic losses are projected using the expected EBITDA loss and, in some individual cases, the FOCF loss. All material risks and the respective countermeasures are documented in the risk management software, which is used throughout the Group. The risk management system is reviewed regularly over the course of the year. Significant changes must be promptly entered in the software and reported to the Board of Management. In addition, a report on the risk portfolio is submitted to the Audit Committee several times a year and to the Supervisory Board at least once a year.

Nonfinancial risks associated with our own business activities, business relations, or products are also recorded. The extent of losses associated with these risks is evaluated on a quantitative and/or qualitative basis. In quantitative evaluation, any potential EBITDA loss is estimated. This also takes into consideration any countermeasures that have a mitigating effect on the potential extent of losses or the probability of the risk. A qualitative assessment of the impact is made on the basis of criteria such as strategic effect, influence on our reputation, or possible loss of confidence among groups of stakeholders.

The following matrix illustrates the quantitative and qualitative criteria for rating a risk as high, medium, or low. The same applies to the classification of nonfinancial risks.

Rating matrix



[1] An individual risk that could have both a direct financial and an indirect financial impact of different severities is always classified based on the higher level of risk.

Process-Independent Monitoring

The effectiveness of our management systems is evaluated at regular intervals by the Corporate Audit function, which performs an independent and objective audit focused on verifying compliance with laws and policies. Corporate Audit also supports the company in achieving its goals by systematically evaluating the efficiency and effectiveness of governance, risk management, and control processes and helping to improve them. This includes internal monitoring of the appropriateness and effectiveness of the internal control system and the risk management system. The selection of audit targets follows a risk-based approach. Corporate Audit performs its duties according to internationally recognized standards. The Supervisory Board's Audit Committee is regularly informed about the results of audits and also receives an annual report on the internal control system and its effectiveness.

Risks in the areas of occupational health and safety, plant safety, environmental protection, and product quality are assessed through specific health, safety, environment, energy, and quality (HSEQ) audits.

The external auditor assesses the early warning system for risks as part of its audit of the financial statements, focusing on whether the system is fundamentally suitable for identifying at an early stage any risks that could endanger the company's continued existence so that suitable countermeasures can be taken. The auditor also reports at regular intervals to Covestro AG's Board of Management and the Audit Committee as well as the Supervisory Board on the results of the audit and any weaknesses identified in the internal control system. Audit outcomes are also taken into account in the continuous improvement of our management processes.

Opportunities and Risks

Overall Assessment of Opportunities and Risks

Particularly in the year 2022, Covestro's business environment was severely affected by geopolitical events, such as the Russian war against Ukraine, a rise in inflation trends around the world, higher energy and raw material prices, disrupted global supply chains, and the global acceleration in recessionary trends. However, the overall opportunity and risk position of the Group, has not changed significantly compared to the previous year. The latest assessment of financial and nonfinancial risks shows that none of the risks reported below endanger the company's continued existence. Nor could we identify any risk interdependencies that could combine to endanger the company's continued existence.

Based on our product portfolio, our know-how, and our innovation capability, we are confident that we can use the opportunities resulting from our business practices and successfully master the challenges resulting from the risks stated below.

Opportunities and Risks in General and in the Company's Business Environment

The risks outlined below may have material effects on EBITDA and, in individual cases, the FOCF of our Group within the one-year forecast period. In this context, risks are deemed material if the potential loss to Covestro is estimated at €50 million or more and/or they have at least a moderate potential qualitative impact. The likelihood of occurrence of the risks is used for internal management purposes to define focus areas for the Corporate Risk Committee. The risks are more highly aggregated in this report than in our internal documentation. Various individual risks are combined into risk categories we have defined for this purpose. The following overview shows the levels of risk allocated to the individual risks within each category. A risk category can therefore include more than one weighted risk occurrence level. The order in which the risk categories are listed does not reflect their significance. Unless explicit information to the contrary is provided, the opportunities and risks described below always refer to both segments of Covestro.

Financial opportunities and risks that affect neither EBITDA nor FOCF are presented separately at the end of the chapter.

Risk management considers risks that could threaten the attainment of the Group's objectives by having a negative impact on the existing business or strategic goals. They are included in our risk portfolio, which is in turn linked to the material sustainability topics and the topics of the Task Force on Climate-related Financial Disclosures (TCFD).

+ Additional information is available at: www.covestro.com/tcfd22

Risk categories by weighted risk occurrence

	Weighted risk occurrence		
Risk categories...	**Low**	**Medium**	**High**
...in the business environment			
Geopolitical tensions and social upheavals		●	
Market development	●	●	
Laws and regulations		●	
...in the company-specific environment			
Procurement	●	●	
Information security, data protection, and information technology (IT)	●	●	
Employees	●		
Production, value creation, and safety	●	●	
Product stewardship	●	●	
Law and compliance	●	●	

● The risk category includes at least one individual risk with this weighted risk occurrence.

Business Environment

Geopolitical Tensions and Social Upheavals

In the year 2022, we saw geopolitical tensions between regional powers, whose effects included a decline in product demand, rising energy and raw material prices, and disruptions in the supply chains. There is great general uncertainty about how existing trade conflicts and tensions will develop, including the associated macroeconomic implications, which could also have an impact on Covestro's business situation.

Market Development

General economic conditions worldwide and, in particular, in the geographic regions in which Covestro operates are a significant factor affecting the company's earnings, since their effect on the industries in which Covestro's direct and indirect customers operate affects demand for our company's products.

Negative economic developments triggered by a variety of events may have a negative impact on the global economy and international financial markets in general. As a rule, this also adversely affects the sales markets for our products, which then usually decreases Covestro's sales volumes and earnings. However, the extent of the impact of economic developments on sales volumes and earnings also depends on capacity utilization rates in the industry, which in turn depend on the balance between supply and demand for the industry's products. Downturns in demand lead to reduced sales volumes and, ultimately, to reduced capacity utilization, which negatively impacts margins. Conversely, a positive economic environment characterized by growth and upward trends normally leads to improved business success.

CORPORATE GOVERNANCE

Covestro's corporate governance is characterized by a sense of responsibility as well as ethical principles. Covestro places great importance on responsible corporate governance. This promise to shareholders, business partners, and our employees is based on our commitment to the German Corporate Governance Code (GCGC) and Articles of Incorporation that reflect these standards. In pursuing our business activities, we follow company principles that exceed the requirements of the law and the GCGC. A key concern is combining business success with environmental and social goals, so when making any business decision, we always consider the three dimensions of sustainability – people, planet, profit. The principles guiding our actions, which are also based on these dimensions, are documented in six policies applicable throughout the Group. These provide our employees with guidance in the areas of value creation; sustainability; innovation; employees; health, safety, environment, energy, and quality (HSEQ); and compliance. The standards contained in these policies are mandatory for all employees worldwide.

+ **Additional information is available at: www.covestro.com/en/sustainability/service-downloads/policies-commitments**

The Board of Management and Supervisory Board provide information pertaining to corporate governance in the sections that follow, including a Declaration on Corporate Governance for Covestro AG pursuant to Section 289f and for the Covestro Group pursuant to Section 315d of the German Commercial Code (HGB). Pursuant to Section 317, Paragraph 2, Sentence 6 HGB, the disclosures in the Declaration on Corporate Governance are not included in the financial statement audit.

Declaration on Corporate Governance

Declaration of Conformity by the Board of Management and the Supervisory Board of Covestro AG on the German Corporate Governance Code Pursuant to Section 161 of the German Stock Corporation Act (AktG)

The Board of Management and Supervisory Board issued the Declaration of Conformity with the GCGC pursuant to Section 161 AktG in December 2022:

Declaration of Conformity by the Board of Management and Supervisory Board
of Covestro AG on the German Corporate Governance Code Pursuant to Section 161 AktG

The recommendations of the Commission of the German Corporate Governance Code, as amended on December 16, 2019, published by the Federal Ministry of Justice and Consumer Protection on March 20, 2020 in the official part of the Federal Gazette have been complied with since the last Declaration of Conformity was issued in December 2021. The recommendations of the Commission of the German Corporate Governance Code, as amended on April 28, 2022, published by the Federal Ministry of Justice and Consumer Protection on June 27, 2022 in the official part of the Federal Gazette are being complied with. Covestro AG will continue to comply with these recommendations in the future.

Leverkusen, December 2022

For the Board of Management	For the Supervisory Board
Dr. Markus Steilemann	Dr. Richard Pott

Corporate governance disclosures and supplementary information on the Board of Management and Supervisory Board, along with the declaration of conformity with the GCGC of December 2022 and those of the past five years are published on Covestro's website.

+ Additional information on the declaration of conformity is available at: ww.covestro.com/en/company/management/corporate-governance

Compensation Report/Compensation System

The compensation system applicable to members of the Board of Management, which was approved by the Annual General Meeting (AGM) on April 21, 2022, and the compensation of the members of the Supervisory Board set out in Section 12 of the Articles of Incorporation of Covestro AG, which was also approved by the AGM on April 21, 2022, are available on our website. The Compensation Report, the auditor's report in accordance with Section 162 Paragraph 3 AktG, and the corresponding results of the latest AGM are also made accessible there. The Compensation Report for fiscal 2022 is also part of this Annual Report.

+ Additional information is available at: www.covestro.com/en/company/management/corporate-governance

Composition, Duties and Activities of the Board of Management and Supervisory Board

Board of Management

Duties and Activities of the Board of Management

The Board of Management runs the company on its own responsibility with the goal of sustainably increasing the company's enterprise value and achieving defined corporate objectives. In doing so, it takes into account the interests of shareholders, employees, and other stakeholders. The Board of Management performs its duties according to the law, the Articles of Incorporation, the Board of Management's rules of procedure, and the recommendations of the GCGC as stated in the Declaration of Conformity. It ensures compliance with the law and internal company policies, and works with the company's other governance bodies in a spirit of trust.

+ The current rules of procedure of the Board of Management are available at: https://www.covestro.com/rulesofprocedure2022

The Board of Management defines the long-term goals and strategy for the company and sets forth the principles and policies for the resulting corporate policies. Furthermore, it coordinates and monitors the most important activities, defines the company's portfolio, develops and deploys managerial staff, allocates resources, and decides on the management and reporting of the Covestro Group. In this context, the Board of Management ensures that both, the risks and opportunities for the company associated with social and environmental factors, and the ecological and social impact of the company's activities are systematically identified and assessed. In addition to the long-term economic goals, the corporate strategy also takes ecological and social goals into account. Corporate planning incorporates appropriate financial and sustainability-related goals.

During their period of service for Covestro, Board of Management members are subject to a comprehensive non-compete clause. They are obligated to work in the company's interests at all times and may not pursue any personal interests in making decisions for the company or take advantage of the company's business opportunities for themselves. All Board of Management members are required to disclose any conflicts of interest to the Chair of the Supervisory Board's Human Resources Committee and the Board of Management Chair, and inform the other Board of Management members of this fact. Other duties, particularly holding seats on Supervisory Boards or comparable governing bodies at companies outside the Group, may only be assumed with the approval of the Supervisory Board.

The members of the Board of Management bear joint responsibility for running the business as a whole. However, the individual members manage the areas assigned to them on their own responsibility within the framework of the decisions made by the full Board. The allocation of duties among the members of the Board of Management is defined in a written schedule appended to its rules of procedure and listed in the following table. The full Board of Management makes decisions on all matters of fundamental importance and in cases where a decision of the full Board is prescribed by law or otherwise mandatory. The rules of procedure of the Board of Management contain a list of topics that must be dealt with and resolved by the full Board.

Board of Management meetings are held regularly and are convened by the Chair of the Board of Management. Any member of the Board of Management may also request that a meeting be convened, notifying the other members of the matter for discussion. The Board of Management makes decisions by a simple majority of the votes cast, except where unanimity is required by law. In the event of a tie, the Chair casts the deciding vote.

According to the Board of Management's rules of procedure, the Chair bears particular responsibility for functional coordination of all Board of Management areas. The Chair represents the Board of Management as well as Covestro AG and the Group in dealings with the public and other third parties.

Compliance

Compliance Management System

Our corporate conduct is characterized by a sense of responsibility as well as ethical principles. Compliance with legal and regulatory requirements is integral to our operations. It is only in this manner that we can sustainably increase the company's enterprise value and safeguard our reputation.

Compliance Culture and Targets

In its Corporate Compliance Policy, Covestro has specified a Group-wide code of conduct that mandates fundamental principles and rules for all employees. This code of conduct details our commitment to fair competition, integrity in business dealings, the principles of sustainability and product stewardship, data protection, upholding of foreign trade and insider dealing laws, the separation of business and private interests, proper record-keeping and transparent financial reporting, as well as to providing fair, respectful, and nondiscriminatory working conditions. These requirements apply within the company as well as to all interactions with external partners and the general public. Our code of conduct provides a framework for all decisions by the company and our employees. The Corporate Compliance Policy is available on our intranet and on our website, and is part of an information packet distributed to new employees when they are hired.

+ Additional information is available at: www.covestro.com/en/company/profile/procurement/sustainability-in-procurement/supplier-code-of-conduct

Covestro is aware that employees will likely embrace and exhibit integrity if managers are excellent role models. The Board of Management states very clearly in its Corporate Compliance Policy for all staff that, above and beyond any legal requirements, Covestro elects not to conduct any business activities that would violate our rules and that management staff is prohibited from instructing employees otherwise. In this way, management continuously fosters our compliance culture by, for example, regularly drawing employees' attention to compliance topics and their significance to the company. At Covestro town hall meetings, for example, Board of Management members regularly present recent compliance cases to employees and underscore the importance of complying with statutory requirements and internal regulations.

↪ See "Corporate Commitments."

We want to utilize our compliance management system in order to:

- Foster and reinforce conduct per compliance requirements,
- Minimize or even eliminate compliance violations,
- Identify risks for potential violations,
- Implement preventive measures, and
- Uncover, halt, and proactively eliminate a repeat occurrence of any compliance violations committed by individuals acting without authorization and in breach of clear rules.

We have taken steps to meet our targets, including implementing an internal control system to ensure compliance rules are followed. The insights gained from our annual evaluation of effectiveness are leveraged in our efforts to continually improve our compliance management system.

→ See "Internal Control System to Ensure Compliance."

Compliance Organization

The Chief Compliance Officer is in charge of all compliance activities at Covestro, and in this function reports directly to the Board of Management. The corporate Law, Intellectual Property & Compliance function is the single point of contact that coordinates Group-wide compliance activities. Chaired by the Chief Financial Officer (CFO) of Covestro, the Compliance Committee is the Group's top-level decision-making body on these issues. The Committee's responsibilities include the following: exercising a Group-wide compliance governance function, initiating and approving compliance-related regulations, and approving the annual training plan. In the reporting period, the Compliance Committee met a total of four times. The suitability and effectiveness of compliance activities are regularly reviewed by the Corporate Audit function in independent, objective audits.

→ See "Process-Independent Monitoring."

Data privacy is under the responsibility of the corporate Law, Intellectual Property & Compliance function and is coordinated Group-wide. By defining controls and processes, the function works to ensure compliance with legal requirements (in particular the EU General Data Protection Regulation, GDPR) and legal judgments to protect personal data of employees, as well as of business partners, media representatives, etc. Local Data Privacy Officers have been appointed for each country in which Covestro has employees. They serve as local points of contact for employees on all questions regarding data privacy. The Board of Management is informed regularly about activities in the company relating to data privacy law.

A local Compliance Officer has also been appointed for each country in which Covestro has employees. This person serves as a local point of contact for employees on all questions regarding legally and ethically correct conduct in business situations. The country organizations also have local compliance committees.

Communications and Compliance

Covestro systematically conducts training courses on compliance. Once focus areas have been specified, target groups are defined for each content category and the employees (including managerial staff) are invited.

Covestro expressly encourages its employees to openly address any doubts about proper conduct in business situations and to solicit advice. We inform all employees whom they can contact if they have any doubts or questions. Covestro has also set up a whistleblowing tool. Employees and third parties can report potential compliance violations through a hotline accessible worldwide or use an online tool that also permits anonymous reports. In addition, employees can also report any compliance incidents to their supervisors or to the Compliance organization.

+ Additional information is available at: www.covestro.com/en/company/management/compliance

An internal policy sets out the principles for handling compliance incidents at Covestro. All suspected compliance incidents are recorded in a central database. Confirmed violations are evaluated, and organizational, disciplinary, or legal measures are taken if necessary.

Compliance incidents are regularly reported to the Supervisory Board, the Board of Management, and the business entities' management teams. Moreover, a current overview of incidents, including additional information on various aspects and developments related to this topic, is published in a monthly Compliance Telegram on the intranet. This ensures a high degree of transparency for all employees.

On a quarterly basis, all companies document risks arising from pending or current legal or administrative proceedings. Relevant cases are reported on a regular basis to the Board of Management and to the Audit Committee of the Supervisory Board. The material legal risks are disclosed in the Notes to the Consolidated Financial Statements.

→ See note 26 "Legal Risks" in the Notes to the Consolidated Financial Statements.

DISCLOSURES ON SUSTAINABILITY REPORTING AND GRI INDEX

Covestro aims to help protect the environment, conserve limited resources, advance society, and create value, all by firmly integrating sustainability into our Group strategy and management.

Our sustainability reporting is based on recognized standards. We report on material topics and nonfinancial performance indicators pursuant to Section 315 (3) of the German Commercial Code (HGB) in our Group Management Report and supplement this information with additional content, which meets the requirements of the “with reference to” reporting option of the Global Reporting Initiative’s (GRI) Sustainability Reporting Standards (SRS); this option has been available since the year 2022. We voluntarily report the management approaches for material topics in accordance with GRI 3-3 (2021). We plan to check whether the use of voluntary GRI reporting under the “in accordance with GRI” option is appropriate against the backdrop of regulatory developments.

Nonfinancial Group Statement

We publish the nonfinancial Group statement pursuant to Sections 315b and 315c in conjunction with Sections 289c through 289e HGB as an integrated part of the Group Management Report. The respective sections include the strategies we pursue in addressing environmental, labor, and social issues as well as protecting human rights and fighting corruption and bribery, including the due diligence processes followed and measures implemented, as well as the outcomes of these strategies.

We applied the GRI standards as a framework for preparing the nonfinancial Group statement.

Key topics relevant to the nonfinancial Group statement are identified in an internal process and in consideration of their significance and implementation within the company. The starting point for this is the materiality assessment and the material sustainability topics identified or updated as a result, i.e., the topics that are of medium or high relevance to Covestro and on the aspects of which Covestro’s business activities have a medium or high impact. The following table provides an overview of the key sustainability topics with an eye to the relevant aspects and contains references to the specific sections in the Group Management Report. In order to identify and address current developments and sustainability-related opportunities and risks at an early stage, we also review whether there are any new findings relevant to opportunity and risk management. No material risks have been identified in connection with Covestro’s own business activities, business relationships, or products that have or are very likely to have a severely negative impact on the nonfinancial aspects of the company’s business.
→ See “Opportunities and Risks Report.”

Key sustainability topics of the Group's nonfinancial statement (HGB)

Key topics of the Group's nonfinancial statement (German Commercial Code)	Relevant aspects in accordance with the Group's nonfinancial statement (German Commercial Code)	Section reference in the Group Management Report
Circular economy	Environmental matters, social matters	"Strategy," "Circular Economy," "Innovation."
Climate neutrality	Environmental matters, social matters	"Strategy," "Management," "Climate Neutrality."
Sustainable R&D based innovation portfolio	Environmental matters, social matters	"Management," "Innovation."
Sustainable products & product stewardship	Environmental matters, social matters	"Strategy," "Sustainable Products and Product Stewardship."
Employer attractiveness	Employee matters	"Employees."
Compliance	Environmental matters, fighting corruption and bribery, respect for human rights	"Opportunities and Risks Report," "Compliance."
Diversity, equity & inclusion	Employee matters, respect for human rights, social matters	"Employees."
Inclusive business	Social matters	"Social Responsibility."
Human rights	Respect for human rights, social matters	"Social Responsibility."
Sustainability in sourcing	Environmental matters, social matters, fighting corruption and bribery, respect for human rights	"Procurement," "Sustainability in the Supply Chain."
Health & safety	Employee matters, environmental matters, social matters	"Integrated Management System for Health, Safety, Environment, Energy, and Quality," „Health & Safety."

As an integral part of the Group Management Report, the nonfinancial Group statement was audited by the financial statement auditor, KPMG AG Wirtschaftsprüfungsgesellschaft, Düsseldorf (Germany), as part of the audit of the Consolidated Financial Statements based on an expansion of the audit engagement.

A nonfinancial statement or nonfinancial report does not have to be provided at this time for Covestro AG.

For economic activity 3.10 – Manufacture of hydrogen, we potentially make a substantial contribution to the environmental objective of climate change mitigation for selected sites. However, we are not yet able at present to fully meet the stringent quality requirements (e.g., product-related lifecycle assessments [LCAs] that go beyond externally certified methodology assessments) that the EU Taxonomy imposes on the evidence to be provided.

Do No Significant Harm (DNSH)

For an activity to qualify as a substantial contribution to one environmental objective, the EU Taxonomy requires that it does not cause significant harm to the five other environmental objectives. In connection with the environmental objective of climate change mitigation, a climate risk and vulnerability assessment was conducted for activity 3.10 – Manufacture of hydrogen at site level, using Representative Concentration Pathways RCP 2.6, 4.5, and 8.5. With regard to the environmental objective of sustainable use and protection of water and marine resources, a risk assessment was likewise performed to establish any possible environmental damage at site level. For the environmental objective of transition to a circular economy, no criteria had been defined for the economic activity analyzed at the time of publication of this report. As a result, compliance is currently not bound by any criteria. The criteria for ensuring that no significant harm is done for the environmental objective of pollution prevention and control were reviewed in two steps. Employees with the relevant professional expertise examined compliance with the requirements for the environmental objective of climate change mitigation set out in Appendix C of Annex 1 of the Commission Delegated Regulation on climate change mitigation in connection with the specified guidelines and regulations. At the same time, compliance with the emission values in connection with the best available techniques (BATs) was verified for the sites at which products are manufactured with which we make a substantial contribution to meeting the environmental objective of climate change mitigation. Finally, a check was performed at site level to make sure that no significant harm is done to the environmental objective of protection and restoration of biodiversity and ecosystems.

For activity 3.10 – Manufacture of hydrogen, proof could be provided for the environmental objective of climate change mitigation that no significant harm was done to the other five environmental objectives. The only exception is Appendix C of Annex 1 of the Commission Delegated Regulation for the environmental objective of climate change mitigation due to interpretation uncertainty about the provision of evidence, especially in relation to subitem g. Taxonomy-eligible products that either do not make a substantial contribution to meeting the environmental objective of climate change mitigation or cause significant harm to at least one environmental objective are not classified as taxonomy-aligned.

Minimum Safeguards

Article 18 of the Taxonomy Regulation requires companies to establish processes and procedures to ensure compliance with different rules and regulations. They relate in particular to human rights (including labor and consumer rights), corruption and bribery, taxation, and fair competition. These requirements correspond to Covestro's culture, which we have made an integral part of our actions on the basis of existing Corporate Commitments, the Supplier Code of Conduct, and various Group regulations. To ensure compliance with all legal and Group-wide provisions, regulations, guidelines, and standards, including those relevant to the minimum safeguards of the EU Taxonomy, we have implemented processes and controls (e.g., as part of the compliance management system, the internal control system, or the integrated Health, Safety, Environment, Energy and Quality management system).

→ See "Corporate Policies," "Health and Safety," "Sustainability in the Supply Chain," "Human Rights," "Compliance," and note 26 "Legal Risks" in the Notes to the Consolidated Financial Statements.

The review of the minimum safeguards for human rights relates to Covestro's overarching management approach to respecting human rights, and primarily to the risk analysis conducted as part of the human rights due diligence. In addition to the company's own business activities, this also covers our direct suppliers. It also considers the upstream supply chain, especially if there are specific allegations. The comprehensive and ongoing risk analysis covers all of Covestro's own sites, the supply chain, as well as the use phase and end-of-life of our products. Depending on the respective risk assessments, various measures are agreed with the suppliers, e.g., supplier assessments under the TfS initiative* or special human rights training.

→ See "Sustainability in the Supply Chain" and "Human Rights."

In addition, as part of the review to establish compliance with the minimum safeguards, we verified at Group level that no final court judgments have been handed down against Covestro in connection with the above issues. Although no economic activities were reported as taxonomy-aligned in the year 2022, there are no indications based on the review described above to suggest that Covestro does not meet the minimum safeguards under Article 18 of the EU Taxonomy Regulation.

We are planning further activities to be undertaken by our cross-functional Human Rights Task Force, such as additional training for buyers, the completion of guidance for buyers with various measures for suppliers prioritized during the risk analysis, or the introduction of a Group-wide guideline on our human rights-related management system.

Result of the Alignment Check

In fiscal 2022, we did not identify any taxonomy-aligned economic activities associated with the environmental objective of climate change mitigation.

Calculation of Taxonomy KPIs

We calculate taxonomy KPIs and report on the nature of taxonomy-eligible and taxonomy-aligned economic activities in accordance with Article 10(3) and Article 11(3) of the Taxonomy Regulation. We are required to report the share of turnover, capital expenditure (CapEx), and operating expenditure (OpEx) that are generated by taxonomy-eligible and taxonomy-aligned activities. The way in which we define and document these KPIs and run the data queries for the calculations prevents double-counting amounts when allocating turnover, CapEx, and OpEx to our economic activities. Where data could not be definitively allocated or KPIs had to be split between economic activities, we applied allocation models appropriate for the particular process to reflect the technical circumstances in the KPI calculation. The taxonomy KPIs are determined with system support in processes established for the purpose. Validation steps are taken and the data is checked against the figures in the Group's Consolidated Financial Statements to ensure the data is complete and correct. Controls in our Internal Control System are used to support the underlying systems and processes.

→ See "Main Features of the Internal Control System."

Turnover

In order to determine the turnover generated by Covestro from taxonomy-eligible economic activities, we allocated the relevant Covestro products to these activities. The corresponding turnover for fiscal 2022 was then calculated for the identified products and a ratio derived using the Covestro Group's sales reported in the Income Statement (denominator). Turnover generated from the activity of high-efficiency co-generation of heat/cool and power from fossil gaseous fuels is calculated in the same way.

→ See "Covestro Group Consolidated Income Statement."

* STOXX Europe 600 Chemicals: Sector index by index issuer STOXX; the STOXX Europe 600 comprises 600 European companies.

Specific Standard Disclosures

Disclosure number	Disclosure title	Section in Annual Report	Section in supplementary information on sustainability	Explanation/omission
GRI 200 – Economic topics				
GRI 201 – Economic Performance (2016)				
3-3	Management Approach	• Strategy – Group Strategy • Management – Management System		
201-1	Direct economic value generated and distributed	• Consolidated Financial Statements and Notes		
GRI 204 – Procurement Practices (2016)				
3-3	Management Approach	• Company Profile – Procurement • Sustainability – Materiality Assessment • Sustainability in the Supply Chain • Social Responsibility – Human Rights • Opportunities and Risks Report – Opportunities and Risks		
204-1	Proportion of spending on local suppliers	• Company Profile – Procurement		Since our locations in Germany, the United States and China cover most of our procurement volume, the sites located in these countries are referred to as main sites within the meaning of the GRI terminology. Local procurement is regarded as purchasing from suppliers located in the same country as the legal entity they supply.
GRI 205 – Anti-corruption (2016)				
3-3	Management Approach	• Sustainability – Materiality Assessment • Compliance – Compliance Management System	• Management – Corporate Policies	
205-1	Operations assessed for risks related to corruption	• Opportunities and Risks Report – Group-wide Opportunities and Risk Management System • Compliance – Compliance Management System		A risk analysis was conducted for every country/every company in the year 2022. Definition of location of operations as a legal entity.
GRI 206 – Anti-competitive Behavior (2016)				
3-3	Management Approach	• Opportunities and Risks Report – Opportunities and Risks • Compliance – Compliance Management System	• Management – Corporate Policies	
206-1	Legal actions for anti-competitive behavior, anti-trust, and monopoly practices			No actions were reported through internal reporting in fiscal 2022.
GRI 207 – Tax (2019)				
3-3	Management Approach		• Compliance – Tax Compliance	
207-1	Approach to tax		• Compliance – Tax Compliance	
207-2	Tax governance, control, and risk management	• Opportunities and Risks Report – Group-wide Opportunities and Risk Management System	• Compliance – Tax Compliance	
207-3	Stakeholder engagement and management of concerns related to tax	• Compliance – Compliance Management System	• Compliance – Tax Compliance	
207-4	Country-by-country reporting			A country-by-country report is not currently provided.

Financial Liabilities

Financial liabilities generally comprise primary financial liabilities and negative fair values of derivatives.

In subsequent periods, such nonderivative liabilities are measured at amortized cost using the effective interest method. The Covestro Group does not opt to measure financial liabilities at fair value, e.g., to avoid or minimize accounting mismatches.

Financial liabilities are derecognized when the contractual obligation is discharged or canceled, or has expired.

Netting Financial Instruments

Financial assets and financial liabilities in the context of master netting or similar agreements are netted and the net amount is recognized in the consolidated statement of financial position if the Covestro Group has a present legal entitlement to offset the recognized amounts against one another and there is the intention to balance them on a net basis or at the same time to settle the corresponding liability with realization of the asset.

Provisions for Pensions and Other Post-Employment Benefits

Within the Covestro Group, post-employment benefits are provided under defined contribution and defined benefit plans. In the case of defined contribution plans, the company pays contributions to publicly or privately administered pension plans on a mandatory, contractual, or voluntary basis. Once the contributions have been paid, the company has no further payment obligations. The regular contributions constitute expenses for the year in which they are due. As such, they are included in the functional cost items, and thus in EBIT. All other post-employment benefit systems are defined benefit plans, which may be either unfunded, i.e., financed by provisions, or funded, i.e., financed through pension funds.

The present value of the defined benefit obligations and the resulting expense are calculated in accordance with IAS 19 (Employee Benefits) using the projected unit credit method. The future benefit obligations are valued by actuarial methods and spread over the entire employment period on the basis of specific assumptions regarding beneficiary structure and the economic environment. These relate mainly to the discount rate, future salary and pension increases, variations in health care costs, and mortality rates.

The discount rates used are calculated from the yields of high-quality corporate bond portfolios in specific currencies with cash flows approximately equivalent to the expected disbursements from the pension plans. The uniform discount rate derived from this interest rate structure is thus based on the yields, on the closing date, of a portfolio of corporate bonds with at least an AA or AAA rating whose weighted residual maturities approximately correspond to the duration necessary to cover the entire benefit obligation.

The fair value of plan assets is deducted from the present value of the defined benefit obligation for pensions and other post-employment benefits to determine the net defined benefit liability. Plan assets in excess of the benefit obligation are reflected in other receivables, subject to the asset ceiling specified in IAS 19. Comprehensive actuarial valuations for all major plans are performed annually as of December 31.

The balance of all income and expenses relating to defined benefit plans, except the net interest on the net liability, is recognized in EBIT. The net interest is reflected in the financial result.

The effects of remeasurements of the net defined benefit liability are reflected in other comprehensive income. They consist of actuarial gains and losses, the return on plan assets, and changes in the effects of the asset ceiling, less the respective amounts included in net interest for the last two components. Deferred taxes relating to the effects of remeasurements are also recognized in other comprehensive income.

Other Provisions

Other provisions are measured in accordance with IAS 37 (Provisions, Contingent Liabilities and Contingent Assets) or, where applicable, IAS 19 (Employee Benefits). Where the cash outflow to settle an obligation is expected to occur after one year, the provision is recognized at the present value of the expected cash outflow. Claims for reimbursements from third parties are separately recognized in other receivables if their realization is virtually certain.

If the projected obligation declines as a result of a change in the estimate, the provision is reversed by the corresponding amount and the resulting income generally recognized in the functional cost item(s) in which the original charge was recognized.

To enhance the information content of the estimates, certain provisions that could have a material effect on the net assets, financial position, and results of operations are selected and tested for their sensitivity to changes in the underlying parameters using sensitivity analysis. To reflect uncertainty about the likelihood of the assumed events actually occurring, the impact of a five-percentage-point change in the probability of occurrence is examined in each case.

Provisions for environmental protection are recognized if future cash outflows are likely to be necessary to ensure compliance with environmental regulations or to carry out remediation work based on an obligation, such costs can be reliably estimated, and no future benefits are expected from such measures.

Estimating the future costs of environmental protection and remediation involves many uncertainties, particularly with regard to the status of laws, regulations, and the information available about conditions in the various countries and at the individual sites. Significant factors in estimating the costs include previous experiences in similar cases, the conclusions in expert opinions obtained for existing environmental programs, current costs, and new developments affecting these costs. Also taken into consideration are management's interpretation of current environmental laws and regulations, the number and financial position of third parties that may become obligated to participate in any remediation costs on the basis of joint liability, and the remediation methods likely to be deployed. Changes in these assumptions could impact future reported results.

Taking into consideration experience gained to date regarding environmental matters of a similar nature, Covestro's management believes the existing provisions to be adequate based upon currently available information. Given the business environment in which the Covestro Group operates and the inherent difficulties in accurately estimating environmental liabilities, material additional costs beyond the amounts accrued may be incurred under certain circumstances. It may transpire during remediation work that additional expenditures are necessary over an extended period and that these exceed existing provisions and cannot be reasonably estimated.

Provisions for restructuring are based either on a legal or a constructive external obligation. They only cover expenses that arise directly from restructuring measures, are necessary for restructuring, and are not related to future business operations. Such expenses include severance payments to employees and compensation payments in respect of rented property that can no longer be used. Prior to recognition of this type of provision, the associated assets are tested for impairment.

Restructuring measures may include the sale or termination of business units, site closures, relocations of business activities, leveraging of portfolio synergies, or fundamental reorganizations of business units. The respective provisions are recognized when a detailed restructuring plan has been drawn up, resolved by the responsible decision-making level of management, and communicated to the affected employees and/or their representatives. Provisions for restructuring are generally recognized at the present value of future cash outflows.

As a company with international operations, the Covestro Group is exposed to numerous legal risks for which provisions for litigation must be recognized under certain conditions – especially in the areas of product liability, competition and antitrust law, patent disputes, tax law, environmental law, and compliance issues such as corruption and export control.

Litigation and other judicial proceedings often raise complex issues and are subject to many uncertainties and complexities including, but not limited to, the facts and circumstances of each particular case, the jurisdiction in which each suit is brought, and differences in applicable law. The outcomes of currently pending and future proceedings generally cannot be predicted. Judgment in court proceedings, regulatory decisions, or the conclusion of a settlement may result in the Covestro Group incurring charges for which no accounting measures have been taken for lack of reasonable estimate or which exceed established provisions and insurance coverage.

The Covestro Group considers the need for accounting measures in respect of pending or future litigations, and the extent of any such measures, on the basis of the information available to its Law, Intellectual Property & Compliance corporate function and in close consultation with legal counsel acting for the Covestro Group.

Where it is more likely than not that such litigation will result in an outflow of resources that is already reasonably estimable, a provision for litigation is normally recognized in the amount of the present value of the expected cash outflows. Such provisions cover the estimated unavoidable payments to the plaintiffs, court and procedural costs, attorney costs, and the cost of potential settlements.

It is often impossible to reliably determine the existence of a present obligation or reasonably estimate the probability that a potential outflow of resources will result from pending or future litigation. Due to the special nature of these litigation, provisions are generally not established until initial settlements allow an estimate of potential amounts or judgments have been issued, and not before at least a range of possible legal outcomes of such litigations can be determined. Provisions for legal defense costs are recognized if it is probable that material costs will have to be incurred for external legal counsel to defend the company's legal position and an outflow of resources can generally be expected.

Internal and external legal counsels evaluate the current status of the material legal risks to the Covestro Group at the end of each reporting period. The need to recognized or adjust a provision and the amount of the provision or adjustment are determined on this basis. Adjusting events are reflected up to the date of preparation of the consolidated financial statements.

→ See note 26 "Legal Risks."

Personnel-related provisions are mainly those recorded for variable one-time payments, individual performance awards, long-service awards, severance payments in connection with early retirement arrangements, surpluses on long-term accounts, and other personnel costs. Since January 1, 2022, calculation of the provision for short-term variable compensation ("Covestro Profit Sharing Plan", "Covestro PSP") has been based not only on the achievement of financial performance indicators such as Earnings Before Interest , Taxes, Depreciation and Amortization (EBITDA), Free Operating Cash Flow (FOCF), and Return on Capital Employed (ROCE) above Weighted Average Cost of Capital (WACC), but also on a sustainability component measured on the basis of selected environmental, social, and governance (ESG) criteria. In fiscal 2022, measurement was based on selected environmental criteria.

Obligations under share-based compensation programs that provide for awards payable in cash are also included in personnel-related provisions ("Prisma"). The compensation of the Board of Management of Covestro AG and of managerial employees includes cash compensation based on the share price that are earned with lock-up periods and are reflected in profit or loss as personnel expenses in line with the consideration paid in the performance period. They are measured using a subscription price model at the time of granting and at each reporting date in accordance with IFRS 2 (Share-based Payment). In 2021, Prisma was expanded to include a sustainability component that covers Covestro's target for reducing greenhouse gas emissions (CO_2 equivalents, CO_2e).

Miscellaneous provisions include those for other liabilities, for product liability, for warranty, and insurance payments. Rebates to be granted to customers, on the other hand are reported under refund liabilities.

Other Receivables and Liabilities

Other receivables are measured at fair value plus the transaction costs directly attributable to the acquisition of the asset.

Pending Transactions

Pending transactions relating to contributions in kind ("executory contracts"), i.e., agreements in relation to which (to a degree) neither the service nor the consideration has been rendered, are not recognized in the statement of financial position on the reporting date if there is no risk of a loss on the reporting date. If there is the risk of a loss, this is generally anticipated in the form of provisions if all the other requirements are met. In contrast, gains anticipated from such agreements on the reporting date may not be recognized in the statement of financial position. Examples of executory procurement contracts include contracts regarding the procurement of energy for the operation of production facilities, which also includes what are known as power purchase agreements (PPA) for the procurement of power from renewable energy. In comparison, pending transactions in the area of the application of the rules regarding financial instruments (financial derivatives) are to be recognized on the reporting date in the amount of the negative fair value if a loss is expected and in the amount of the positive fair value if a gain is expected.

Impairment Testing

If there are indications that an individual intangible asset that does not constitute goodwill (other intangible asset) or property, plant and equipment may be impaired, the recoverable amount is compared to the carrying amount to determine whether it is higher or lower. The recoverable amount is generally the higher of the value in use or the fair value less costs of disposal. If the recoverable amount does not exceed the respective carrying amount, an impairment loss is recognized in profit or loss in the amount of the difference between the carrying amount and the recoverable amount. If the reasons for a previously recognized impairment loss no longer apply, the impairment loss is reversed in profit or loss provided that the reversal does not cause the carrying amount to exceed the original (amortized) cost of acquisition or production. Impairment losses and any impairment loss reversals are recognized in the functional cost in the same way as depreciation and amortization, depending on the use of the respective assets.

In addition to impairment testing of individual items of property, plant and equipment and other intangible assets, cash-generating units are globally tested if there is indication of impairment. Recognized goodwill is tested for impairment if there is indication of impairment, but at least once a year. Testing is generally done in the fourth quarter at the level of (groups of) cash-generating units.

A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. As a rule, Covestro considers strategic business entities to be cash-generating units. They represent the reporting level below the seven business entities that form the two reportable segments, Performance Materials and Solutions & Specialties. In cases where recognized goodwill in groups of cash-generating units is tested for impairment annually, the level tested is the relevant business entity.

If recognizing an impairment loss is required at the level of a CGU or group of CGUs, goodwill is written down first. In cases where the necessary impairment loss exceeds the goodwill written down, the remaining charge is distributed across other noncurrent, nonfinancial assets in proportion to their carrying amount. The impairment loss on goodwill is reported in other operating expenses. Impairment losses on goodwill may not be reversed.

The recoverable amount of a CGU or group of CGUs is equal to the fair value less costs of disposal. This calculation is based on the present value of the future cash flows since no market price can be determined for the individual units. The forecasts of future cash flows for determining the recoverable amount are based on the Covestro Group's current planning, which generally extends over 10 years, although a shorter detailed planning period of generally five years is used for assessment purposes. In certain cases, shorter or longer planning horizons are also considered if advisable due to specific assumptions underlying the planning. Assumptions made for purposes of forecasting cash flows mainly concern future selling prices and volumes, costs, market growth rates, economic cycles, and exchange rates. Changes in these assumptions are based on the Group's own estimates and external sources of information. Where the recoverable amount is the fair value less costs of disposal, this is measured from the viewpoint of an independent market participant. Cash flows beyond the detailed planning period are determined on the basis of the respective individual growth rates derived from market information and the associated long-term business expectations. The measurement of fair value less costs of disposal is based on unobservable inputs ("Level 3" of the fair value hierarchy).

The net cash inflows are discounted at the weighted average cost of capital (WACC), which is calculated as the weighted average cost of equity and cost of debt. To take into account the risk and return profile of the Covestro Group, an after-tax cost of capital is calculated, and a specific capital structure is defined via benchmarking against comparable companies in the same industry sector ("peer group"). The cost of equity corresponds to the return expected by shareholders, while the cost of debt is based on the terms at which the peer group can obtain long-term financing. In principle, both components are derived from capital market information.

The monitoring and management structure for recognized goodwill and the capital cost factors and growth rates used in annual impairment testing are presented in the following table for each CGU or group of CGUs. The growth assumptions reflect, in particular, economic cycles over several years as well as expectations for capacity and the market for each unit to be tested.

26. Legal Risks

As a company with international operations, the Covestro Group is exposed to numerous legal risks, particularly in the areas of product liability, competition and antitrust law, patent disputes, tax law, environmental law, and compliance issues such as corruption and export control. The outcome of any current or future proceedings cannot be predicted. It is therefore possible that legal judgments or regulatory decisions or future settlements could give rise to expenses that are not covered, or not fully covered, by insurers' compensation payments and could significantly affect the Covestro Group's earnings.

Legal proceedings currently considered to involve material risks are outlined below. The legal proceedings referred to do not necessarily represent an exhaustive list:

Carbon Monoxide Pipeline from Dormagen to Krefeld-Uerdingen

The carbon monoxide pipeline is intended to connect the chemical production sites at Dormagen (Germany) and Krefeld-Uerdingen (Germany) and complement the network already existing between Dormagen and Leverkusen (Germany). The aim is to ensure a safe and reliable supply of carbon monoxide to and across all sites. Although the pipeline was almost completed by the end of year 2009, it cannot currently be brought into operation because of ongoing court proceedings. Following confirmation by the Düsseldorf Administrative Court in the year 2011 that there were no grounds to challenge the material aspects of the planning permission decision, in particular the safety of the materials used and the legal conformity of the relevant pipeline act (Rohrleitungsgesetz), the plaintiffs and the regional government against which legal proceedings had been instituted lodged appeals before the Higher Administrative Court for the state of North Rhine-Westphalia in Münster (Higher Administrative Court). In the year 2014, the Higher Administrative Court raised no objections in principle to the safety and routing of the pipeline, but questioned the constitutionality of the pipeline act which forms the legal basis for the project. On December 21, 2016, Germany's Federal Constitutional Court dismissed the corresponding constitutionality question referred to it by the Higher Administrative Court as inadmissible and confirmed the legal opinion of the Covestro Group. Subsequently, the Higher Administrative Court again considered the facts of the appeal and, in a decision rendered on August 31, 2020, dismissed the actions against the planning permission decision. In addition, the Higher Administrative Court rejected an appeal against its ruling. The plaintiffs then filed a complaint against the denial of leave to appeal with the Federal Administrative Court in Leipzig in February 2021. The German Federal Constitutional Court dismissed the denial of leave to appeal on December 14, 2021. The judgment by the Higher Administrative Court is therefore final. Seven actions against the planning permission decision are still pending at Düsseldorf Administrative Court which could now proceed on the basis of the final judgment by the Higher Administrative Court.

Civil Class Action Lawsuits over Diisocyanates (in the United States)

On July 9, 2018, Covestro LLC, Pittsburgh, Pennsylvania (United States) – as one of numerous other defendants – was served the first of now 12 class action lawsuits initiated by various U.S. diphenylmethane diisocyanate (MDI) and toluene diisocyanate (TDI) customers. The plaintiffs allege that the defendants have violated various provisions of the Sherman Antitrust Act since January 1, 2015, by acting in coordination to limit production capacities of MDI and TDI and, at the same time, raising prices for these products in the market. On October 3, 2018, the Judicial Panel on Multidistrict Litigation ruled that all class action lawsuits in pretrial proceedings would be centralized in the District Court for the Western District of Pennsylvania. Based in essence on the same assertions and the violations of federal consumer protection and antitrust laws allegedly resulting from them, the attorney general of the state of Mississippi filed a separate civil complaint against Covestro LLC and numerous other defendants on behalf of the state and its citizens in September 2019. In November 2020, the parties suspended these lawsuits without prejudice for a period of two years. Owing to the time which has passed, the suspension of the limitation period agreed at the time with regard to the claims of the state and its citizens expired again in November 2022. Covestro currently considers these claims without merit and will therefore use all legal means to defend itself against these allegations – also in light of the official conclusion in November 2018 of the six-month investigation by the U.S. Department of Justice into possible anticompetitive practices in relation to MDI. The case is currently still in the discovery phase.

Other Information

27. Notes to the Statement of Cash Flows

27.1 Cash Flows from Operating Activities

The net cash inflow from operating activities of €970 million (previous year: €2,193 million) reflects the operating surplus and also takes into account changes in working capital and other noncash transactions.

The year-over-year decrease in cash flows from operating activities of €1,223 million (– 55.8%) was mainly the result of a €1,468 million decrease in EBITDA, which was partially offset by a €214 million reduction in cash outflows from working capital and an €8 million decrease in income tax payments.

27.2 Cash Flows from Investing Activities

Net cash outflow for investing activities in 2022 amounted to €477 million (previous year: €1,995 million).

This was primarily attributable to cash outflows for additions to property, plant, equipment and intangible assets of €832 million (previous year: €764 million) and cash outflows for noncurrent financial assets of €124 million. Cash inflows from other current financial assets in the amount of €374 million (previous year: €188 million) had an offsetting effect. The previous year was characterized, in particular, by cash outflows for acquisitions less cash acquired for the takeover of the RFM business in the amount of €1,469 million.

27.3 Cash Flows from Financing Activities

The net cash inflow from financing activities amounted to €64 million in 2022 (previous year: outflow of €965 million). Net borrowing amounted to €995 million (previous year: net credit repayment in the amount of €624 million). Short-term borrowing and debt repayment were netted.

There was an outflow of €150 million (previous year: €0 million) in 2022 for the acquisition of treasury shares as part of Covestro AG's share buyback program. The issuance of treasury shares concerns shares (€8 million) (previous year: €2 million) issued to employees in the context of the Covestment share-based participation program.

In April 2022, a dividend totaling €651 million (previous year: €251 million) was paid to Covestro AG shareholders.

The interest paid totaling €131 million (previous year: €81 million) reflected in cash flows from financing activities relates mainly to forward exchange contracts used to hedge foreign currency risks of €63 million (previous year: €20 million), lease liabilities of €25 million (previous year: €26 million), and bonds of €23 million (previous year: €23 million).

Reconciliation of financial debt in fiscal 2022

			Noncash changes					
	Carrying amounts Dec. 31, 2021	Cash changes	Changes due to exchange rate movements	Changes in measure-ment	Acquisitions (IFRS 3)	Lease contracts	Other changes	Carrying amounts Dec. 31, 2022
	€ million	€ million	€ million	€ million	€ million	€ million	€ million	€ million
Bonds	1,492	494	–	2	–		–	1,988
Liabilities to banks	275	652	(5)	–	–		–	922
Lease liabilities	761	(160)	14	–	–	131	–	746
Other financial liabilities	2	9	–	–	–		(10)	1
Financial debt[1]	**2,530**	**995**	**9**	**2**	**–**	**131**	**(10)**	**3,657**

[1] Excluding forward exchange contracts used to hedge currency risks