
CORPORATE GOVERNANCE

VALUE ENHANCEMENT THROUGH RESPONSIBLE BALANCING OF INTERESTS

LEGAL FRAMEWORK

schlott gruppe AG is a corporation organized under the laws of the Federal Republic of Germany. It is subject to the legal provisions governing the management and control of corporations. The Board of Management and the Supervisory Board are responsible for the administration of corporations. The statutes of *schlott gruppe AG* reflect the standards established and subscribed to by German commerce and industry. The management and supervision of the Corporation are based on the German Code of Corporate Governance.

CORPORATE GOVERNANCE-PHILOSOPHY OF THE SCHLOTT GROUP

The corporate statutes of *schlott gruppe AG* do not contain any rules and provisions, which deviate in a marked way from general market standards in Germany. This applies particularly to the rights of shareholders, which are observed to the fullest extent – all shareholders are treated equal in line with legal regulations. This applies also to the purchase of own shares and to acquisitions. The shareholders of *schlott gruppe AG* are guaranteed the basic participation in corporate earnings, the unimpeded purchase and sale of shares of the Corporation and identical voting rights for each basic share. All shares issued by *schlott gruppe AG* are of the same type with uniform shareholder rights.

The Board of Management recognizes that shareholders of *schlott gruppe AG* as owners of the Corporation provide capital for growth and thus participate in the entrepreneurial risk. The Board is, therefore, especially indebted to shareholders. In view of this, our management philosophy is characterized by comprehensive, timely and transparent communication taking into consideration competitive factors. It is further characterized by modern and efficient risk management, observance of exchange regulations and by a management that sets as the most important goals the ongoing and strategic enhancement of the value of the Corporation.

Consistent value enhancement is, however, only possible if the Corporation is managed in such a way that the interests of all stakeholders are being observed. Stakeholders, aside from shareholders, are customers, employees,

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debtors and all other business partners. Therefore, the management of the *schlott group* is guided by the need to consider the interests of all stakeholders.

Beyond the reporting and disclosure requirements legally mandated (annual and quarterly reports, events requiring ad hoc reports, Directors' dealings and changes in the shareholder structure), the *schlott group* reports regularly in accordance with the required equal treatment of all shareholders ("fair disclosure") on trends in the Corporation by means of press releases and conferences with analysts, the press and shareholders. All reports and information provided, as well as the major presentations at conferences, are being published on the Internet under *www.schlottgruppe.de*.

INTERACTION BETWEEN THE BOARD OF MANAGEMENT AND THE SUPERVISORY BOARD

The *schlott group* has set forth in a policy statement the tasks of and the interrelationship between the Board of Management and the Supervisory Board. These policy statements, and in particular the rights and responsibilities of the Members of the Supervisory Board and the Board of Management, were formulated and adopted in line with the requirements contained in the German Code of Corporate Governance.

While acting as Members of the Board of Management, Members are subject to far-reaching non-competition clauses. Additional business activities of Members, particularly the acceptance of memberships on supervisory boards, require always the consent of the Supervisory Board. The same applies to extension of credit by the Corporation to Members of the Board of Management or the Supervisory Board.

The rights and responsibilities under the Code of Corporate Governance are part of the statutes of the Supervisory Board to the extent that no deviations from the Code were declared. It was further defined that Members of the Supervisory Board, who are also members of management boards of publicly-traded corporations, may not assume more than five mandates on supervisory boards of publicly-traded corporations outside of the corporation for which they are members of the management board.

The Supervisory Board may not have more than two former Members of the Board of Management, nor may Members of the Supervisory Board be involved in official functions or consulting roles with major competitors of the Corporation.

COMPENSATION OF THE MEMBERS OF THE BOARD OF MANAGEMENT

The compensation of Members of the Board of Management consists of fixed parts and performance-related payments. In addition, Members receive benefits in-kind as well as retirement benefits. Stock options or similar constructions were not issued.

This variable compensation includes incentives for increasing the valuation of the Corporation. A major element in the valuation of an enterprise by the capital markets is the dependability in terms of achieving goals and expectations. That is why the amount of performance-related compensation for Members of the Board of Management is directly tied to the achievement of the prognosticated results of the Corporation (EBT), aside from individually agreed performance criteria. The less than satisfactory earnings trends during the past fiscal year are reflected in the amount of performance-related compensation.

Furthermore, incentives exist for optimizing the balance sheet structure in addition to reaching EBT goals. To this effect, the *schlott group* has developed a detailed proprietary concept for the control and optimization of its balance sheet structure. Depending on each stage of an acquisition cycle, goals and limits as to indebtedness were defined and had to be reached and complied with.

EBT and the coverage of the cost of capital are the central steering mechanisms of the Corporation in its implementation of its strategic goals, particularly the active shaping of the European intaglio printing industry. The performance criteria and incentives for the Board of Management are therefore directly and clearly derived from the strategic direction of the *schlott group*. During the business year 2005/06, the total compensation for the Board of Management amounted to € 1.3 million, of which € 0.2 million were performance-related.

COMPENSATION OF THE MEMBERS OF THE SUPERVISORY BOARD

During the past year, the Members of the Supervisory Board received for their services a total of € 236,250.00. The 2006 Annual General Meeting resolved to grant additional compensation to Members of Committees of the Supervisory Board. Such payments totaled € 40,000.00 during the reporting year. This amount is included in the above overall total. Moreover, travel expenses incurred were reimbursed. The individual compensation amounts were € 15,000.00 for Members, € 30,000.00 for the Chairman and € 22,500.00 for the Deputy Chairman. Nikolas Broschek, Member of the Supervisory Board, received a consulting fee of € 60,000.00 (€ 30,000.00 in the previous year).

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SHARE OWNERSHIP OF THE BOARDS AS OF DECEMBER 31, 2006

SHARE OWNERSHIP BOARD OF MANAGEMENT	50,090
SHARE OWNERSHIP SUPERVISORY BOARD	1,880,230
of which:	
<i>Nikolaus Broschek</i>	457,688
<i>Erwin J. Kiefer (indirectly via related Elke Kiefer via EKS Beteiligungs-GmbH)</i>	565,000
<i>Sigmund Kiener (indirectly via S.K. Management- und Beteiligungs GmbH)</i>	287,542
<i>Joachim Kohm (indirectly via JUST-US GmbH)</i>	570,000
TOTAL NUMBER OF SHARES	6,204,200

SHARE OWNERSHIP OF BOARDS

The share ownership of Members of the Supervisory Board is illustrated above. No Member of the Board of Management owns more than one percent of the capital stock, thus making an individual breakdown unnecessary.

During the reporting year, the transactions stated in the following table required public notification as per article 15a WpHG.

Directors' Dealings (article 15a WpHG) October 1, 2005 to December 31, 2006

<i>Name</i>	<i>Function</i>	<i>Date of Notification</i>	<i>Type</i>	<i>Number of Shares</i>	<i>Price in €</i>
Joachim Kohm	Member of the Supervisory Board	11-14-2005	Purchase	10,000	261,000.00
S.K. Vermögensholding GmbH	Connection to a Member of the Supervisory Board	11-21-2005	Purchase	22,500	590,186.25
S.K. Vermögensholding GmbH	Connection to a Member of the Supervisory Board	11-21-2005	Purchase	2,776	73,008.80
Joachim Kohm	Member of the Supervisory Board	06-30-2006	Purchase	10,000	203,500.00
Joachim Kohm	Member of the Supervisory Board	06-30-2006	Purchase	5,000	104,250.00
S.K. Management- und Beteiligungs GmbH	Connection to a Member of the Supervisory Board	07-03-2006	Purchase	10,000	204,500.00
S.K. Management- und Beteiligungs GmbH	Connection to a Member of the Supervisory Board	07-03-2006	Purchase	1,000	20,950.00
S.K. Management- und Beteiligungs GmbH	Connection to a Member of the Supervisory Board	07-07-2006	Purchase	4,000	86,384.00
S.K. Management- und Beteiligungs GmbH	Connection to a Member of the Supervisory Board	07-07-2006	Purchase	3,968	86,105.60
S.K. Management- und Beteiligungs GmbH	Connection to a Member of the Supervisory Board	08-07-2006	Purchase	5,998	139,657.43

<i>Name</i>	<i>Function</i>	<i>Date of Notification</i>	<i>Type</i>	<i>Number of Shares</i>	<i>Price in €</i>
Joachim Kohm	Member of the Supervisory Board	08-14-2006	Sale	515,000	11,082,800.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	08-14-2006	Purchase	515,000	11,082,800.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	08-17-2006	Purchase	5,000	109,500.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	08-17-2006	Purchase	5,000	109,750.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	08-28-2006	Purchase	5,000	108,450.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	08-28-2006	Purchase	5,000	108,850.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	08-29-2006	Purchase	5,000	109,000.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	08-30-2006	Purchase	10,000	217,380.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	08-31-2006	Purchase	5,000	107,850.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	09-01-2006	Purchase	5,000	108,250.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	09-11-2006	Purchase	5,000	108,000.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	09-12-2006	Purchase	4,400	95,700.00
JUST-US GmbH	Connection to a Member of the Supervisory Board	09-14-2006	Purchase	600	13,536.00
S.K. Management- und Beteiligungs GmbH	Connection to a Member of the Supervisory Board	09-19-2006	Purchase	17,542	400,308.44

DECLARATION OF COMPLIANCE AS PER ARTICLE 161
GERMAN CORPORATION ACT (AKTG)

The Board of Management and the Supervisory Board of *schlott gruppe AG* have agreed on the following declaration as per article 161 of AktG:

The *schlott gruppe Aktiengesellschaft* represents that since the issuance of the last Declaration of Compliance on May 30, 2006, it has complied with all the recommendations made by the “Federal Commission of the German Corporate Governance Code” published in the official part of the electronic Bundesanzeiger of the German Ministry of Justice, based on the version dated July 20, 2005, with the following exceptions: there is no deductible under the Directors-and-Officers-Liability-Insurance for Members of the Board of Management and the Supervisory Board; compensation of the Board of Management is not shown separately for each Member; Members of the Supervisory Board do not receive any performance-related compensation; *schlott gruppe AG* is not issuing its annual report within ninety days after the end of the fiscal year; the chairmanship in any of the Committees of the Supervisory Board is not being separately compensated. The *schlott gruppe Aktiengesellschaft* complies with all the recommendations made by the “Federal Commission of the German Corporate Governance Code”, based on the version dated June 12, 2006, with the aforementioned exceptions as well as the detailed disclosure of the compensation for Members of the Board of Management, articles 4.2.4 and 4.2.5 of the Code. The *schlott gruppe Aktiengesellschaft* will continue to abide by the recommendations contained in the Code aside from the aforementioned exceptions. However, compensation for Members of the Board of Management will be disclosed on an individual basis.

FREUDENSTADT, JANUARY 12, 2007

THE SUPERVISORY BOARD
OF THE SCHLOTT GRUPPE AG

THE BOARD OF MANAGEMENT
OF THE SCHLOTT GRUPPE AG

REPORT OF THE SUPERVISORY BOARD

SCHLOTT GRUPPE AG

In the following report, the Supervisory Board of *schlott gruppe AG* comments on its activities during the business year 2005/06. In particular, it will elaborate on the ongoing close coordination with the Board of Management, the major issues deliberated in its meetings, the work of Committees as well as on the audit of the year-end financial statements.

The Supervisory Board has discharged its responsibilities during the reporting year as set forth by law and the statutes of *schlott gruppe AG*. With respect to the management of the Corporation, it has maintained a continuous collaboration with the Board of Management, advised it on an ongoing basis and has supervised the administration of the Corporation. The Supervisory Board was directly involved in all decisions fundamental to the well-being of the Corporation. The strategic positioning of the Corporation was determined in close coordination between the Board of Management and the Supervisory Board.

The Board of Management has informed the Supervisory Board on a regular basis, both orally and in writing, in a comprehensive and timely fashion of all important issues related to current business conditions, the position of the group, tactical planning as well as the further strategic development. On the basis of detailed reports presented by the Board of Management, all issues important to *schlott gruppe AG* were discussed in detail by the Supervisory Board. In addition, the Supervisory Board was given notice at regular intervals of risks encountered, of the state of the risk management system and of counter measures undertaken. Deviations from plans and goals were examined and discussed in detail by the Supervisory Board.

Its meetings' agendas during the reporting year regularly addressed the development of the share price of *schlott gruppe AG* and the reputation and positioning of the Corporation in the capital markets.

Between regularly scheduled meetings of the Supervisory Board, it was advised of important developments on an ongoing basis. As Chairman of the Supervisory Board, I was in continuous contact and dialogue with the Members of the Board of Management.

During the fiscal year 2005/06, the Supervisory Board convened five times. The majority of meetings were attended by all Members. Only Ms. Salberg was absent from more than half of the meetings due to illness.

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CHANGES IN THE COMPOSITION OF THE SUPERVISORY BOARD

On April 30, 2006, Ms. Irene Salberg retired from the Supervisory Board as Member representing employees. Her seat was assumed by Mr. Josef Peitz on October 4, 2006. There were no other changes during the reporting year.

THE WORK OF COMMITTEES

The Supervisory Board has established three Committees as set forth in its statutes. These Committees are chaired by the Chairman of the Supervisory Board. In this function, he has regularly and in a detailed fashion advised the full Board of the workings of the Committees.

The three Committees are the Arbitration Committee in line with article 27, Chapter 3, of the Law of Co-Determination, the Personnel Committee and the Audit Committee. The Committees prepare topics, issues and decisions that are to be considered by the full Board. As per its statutes, the Supervisory Board has delegated various authorities to the Committees.

The membership of the Committees were as follows during the reporting year:

ARBITRATION COMMITTEE:

Erwin J. Kiefer*, Ivan Bebek, Edmund Hug, Michael Schlecht

AUDIT COMMITTEE:

Erwin J. Kiefer*, Ivan Bebek, Reinhold Schreiner, Dr. Herbert Pototzky

PERSONNEL COMMITTEE:

Erwin J. Kiefer*, Ivan Bebek, Nikolaus Broschek, Andrea Raab

* *Chairman*

During the reporting year, there was once again no need to convoke the Arbitration Committee. The Personnel Committee convened twice during the reporting year. Major topics included the determination of the variable components related of the compensation for Members of the Board of Management. The review as to attainment of specified compensation parameters is also part of the responsibilities of the Personnel Committee. Moreover, the Personnel Committee addressed the issue of filling the vacant position of Chief Financial Officer. After careful evaluation of several candidates, the Supervisory Board appointed Mr. Heiko Arnold as a new Member of the Board of Management. After this decision was announced on March 21, 2006, Mr. Arnold assumed his responsibilities on June 1, 2006.

The Audit Committee met once during the reporting year. It addressed primarily the year-end financial statements and basic issues related to the management of risks. Moreover, it issued a mandate for the audit of financial statements, appointed the external auditor and determined the fee for the audit. One of the important tasks of the Audit Committee is to secure and monitor on an ongoing basis the independence of the external auditor. During the reporting year, the Audit Committee has not found any evidence that the independence of the auditor was impaired and the Committee saw no need to take further steps for securing this independence. The external auditor participated in the meeting of the Audit Committee and reported in detail on its audit activities.

WORK OF THE SUPERVISORY BOARD

The regular consultations and deliberations of the Supervisory Board of *schlott gruppe AG* addressed issues such as sales and earnings trends, financial position, capital expenditures as well as employment trends within the group, the various subsidiaries, segments and sites.

In addition, the Board addressed on a regular basis matters concerning Corporate Governance. The Supervisory Board has adopted the Declarations of Compliance in line with article 161 AktG. In its meeting of January 13, 2006, the Supervisory Board deliberated on the compensation of Members of Committees and developed a draft proposal to this effect for the Annual General Meeting. With the Annual General Meeting's decision to adopt the proposal, separate compensation for Members of Committees of the Supervisory Board has been granted. Moreover, the Supervisory Board addressed and examined its own efficiency without the presence of Members of the Board of Management. It also deliberated in detail about the implications for *schlott gruppe AG* arising out of the law dealing

with the improved protection of share investors. The Board of Management speaks also for the Supervisory Board in the statements on Corporate Governance contained in the Annual Report 2005/06 of *schlott gruppe AG*.

Major topics discussed in the Meetings of the Supervisory Board included the further strategic development of the group, especially the long-term investment strategy in the business segment print as well as the current large capital expenditure project at the Freudenstadt site. With regard to this business segment, the short and medium-term trends of the intaglio printing industry, and especially trends in market prices, were important elements in the deliberations of the Board. Furthermore, the acquisition of the *reus group*, the adjustment of depreciation periods of tangible assets in line with the requirements of IAS 16, as well as the development of relevant indicators for return on capital and capital commitments, especially in current assets, were important topics in the discussion on corporate strategy and business development.

In its meeting of January 12, 2007, the Supervisory Board has reviewed in detail the year-end financial statements of the AG (HGB) and the group (IAS/IFRS), as well as the Consolidated Management Report as prepared by the Board of Management. In line with the exemption permitted under article 292a HGB, the group financial statements at year-end were not prepared as per HGB. The corresponding explanations to this effect have been added in the Notes to the financial statements as per IAS/IFRS. AWT AUDIT WIRTSCHAFTS-TREUHAND AG, certified public accountants domiciled in Stuttgart, have examined the annual financial statements of *schlott gruppe AG* and the Consolidated Financial Statements as well as the Consolidated Management Report and have rendered their unqualified opinion.

After careful examination, the Supervisory Board, on the basis of a recommendation of the Audit Committee, approved the results of the audit by the external auditor as well as the year-end financial statements of the *AG* and the *group*, which were thus adopted.

The Supervisory Board in its meeting of January 12, 2007, has concurred with the recommendation of the Board of Management regarding the use of net income for the year. The Supervisory Board and the Board of Management recommend to the Annual General Meeting on March 13, 2007, to distribute a dividend of € 1.00 per common share. During the past business year, the Board of Management and all employees have again performed successfully in a still difficult economic environment. The Supervisory Board wishes to thank all those involved for their extraordinary dedication.

JANUARY 2007



ERWIN J. KIEFER

Chairman of the Supervisory Board