

Financial report 2017

Volkswagen Financial Services N.V.

Amsterdam

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Supervisory Board Report

The balance sheet total and the result for the financial year 2017 of Volkswagen Financial Services N.V. ('FSNV' or 'the Company') are in line with the expected development of the Company.

The solvency and liquidity of the Company remained good. The issuance activities of FSNV in the capital markets were coordinated with the parent company, Volkswagen Financial Services AG.

The diesel issue, which surfaced in 2015, has been addressed by the ultimate group parent company, Volkswagen AG, by entering into settlement agreements with the authorities in the respective countries.

In 2017, Moody's rated Volkswagen Financial Services AG, the parent company, with Prime-2 / A3 (short term / long term) with negative outlook while Standard & Poor's rated Volkswagen Financial Services AG with A-2 / BBB+ (short term / long term) and upgraded the outlook from negative to stable.

The Management Board informed the Supervisory Board in 2017 continuously on the developments regarding issuance activities and risk exposure. Risk limits set by the Supervisory Board were adhered to.

During the Annual General Meeting held on 7 June 2017, BDO Audit & Assurance B.V. was reelected as independent auditors for the fiscal year 2017. The independent auditors audited the annual financial statement of FSNV and issued an unqualified audit opinion.

Amsterdam, 6 March 2018

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Original was signed by
Frank Fiedler, Chairman of the Supervisory Board

Management Report

Business Strategy and Objectives

Volkswagen Financial Services N.V. ('FSNV'), founded in 1983, is one of the funding vehicles of parent company Volkswagen Financial Services AG ('FSAG') and its subsidiaries. FSNV raises funds by issuing bonds and commercial papers in the international capital markets and lends the proceeds to Volkswagen Financial Services companies and joint ventures. FSNV provides the capital market funding as a service within Volkswagen Financial Services Group, thereby achieving an adequate return commensurate with the efforts and associated risks.

Funding

Basis for the issuing activities are the EUR 25 billion Debt Issuance Programme ('DIP') that adheres to the European Prospectus Directive and is regularly updated, as well as the EUR 5 billion Commercial Paper ('CP') Programme. All issuances are fully guaranteed by FSAG.

Therefore, the FSNV rating by Moody's and Standard & Poor's is derived from the FSAG rating. Moody's assessed the risk with Prime-2 / A3 (short/long term) with a negative outlook while Standard & Poor's assessed the rating with A-2 / BBB+ (short/long term) with a stable outlook in 2017.

Throughout 2017, FSNV raised a EUR equivalent of 1.7 billion under the DIP-programme (2016: EUR 0) with multi-tranche bonds and a total EUR equivalent of 1.3 billion with 51 transactions under the mentioned CP Programme (2016: EUR equivalent 2.5 billion). The proceeds were granted to Volkswagen Financial Services Group companies.

In 2017, FSNV also redeemed bonds with a EUR equivalent of 0.9 billion (2016: EUR 1.7 billion) and CPs totalling EUR 1.8 billion (2016: EUR 1.8 billion). Borrowings from VW Group companies amounted to EUR 0.3 billion (2016: EUR 0.1 billion), repayments to EUR 1.5 billion (2016: 0.4 billion).

In 2017, the shareholder contributed EUR 120 million to the share premium reserve (2016: contribution EUR 400 million, repayment EUR 501 million).

Financial results

FSNV generated a profit after tax of EUR 7.2 million in 2017 against EUR 9.5 million in 2016. The Company generates income from the Group financing business. Interest surplus amounted to EUR 11.1 million (2016: EUR 14.4 million) due to reduced financing needs of group companies.

Given that issuances under the DIP and CP-Programmes are guaranteed by FSAG, the overall financial position is sound.

Risks

FSNV is exposed to business and financial risks. Business risks comprise inter alia legal, operational, personnel, reputational and compliance risks. FSNV is adhering to the Governance, Risk and Compliance Guidelines of Volkswagen Financial Services AG managing the aforementioned risks within the Group policies.

The main financial risks of FSNV are liquidity risk, credit risk, currency risk and interest rate risk.

Liquidity risk is defined as the risk of not being able to meet own payment obligations in full or when due.

Credit risk is defined as the risk of incurring losses as a result of a default of a borrower or bank.

Currency risk refers to the potential loss in open currency positions arising from adverse changes in exchange rates.

Interest rate risk occurs because of fixed and floating interest rate mismatches between asset and liability items on the balance sheet.

The Supervisory Board has established narrow risk limits to restrict these risks and achieve a low risk exposure.

Risk policies

Liquidity risk is contained by extending loan amounts sourced from bond or CP-issuances to Volkswagen Financial Services Group companies at identical tenors as the funded amounts. VW Group borrowers repay their loans on the same due date when FSNV's own payment obligations to the capital markets become due.

Credit risk is addressed by monitoring the financial stability of the Group borrowers and external banks. A fair value and impairment trigger assessment is performed for Group companies at least once a year or in case of need. Banks are monitored centrally at Volkswagen Financial Services AG based on rating and financial analyses. Financial transactions are only conducted with approved banks.

Currency risk is limited by matching funding and lending currency amounts. In case funding and lending currency do not match, derivatives are used to achieve closed positions.

Interest rate risk is contained by matching the fixed and floating interest rate terms of the funding and lending amounts. Mismatches are closed using interest rate derivatives.

For remaining mismatches, the Supervisory Board has defined narrow limits. FSNV uses adequate tools to assess and to monitor risks. On a monthly basis, a detailed mismatch report, containing all relevant risks, is presented to the management. In 2017, limits were not exceeded.

Diesel issue

In September 2015, the California Air Resources Board (CARB) and the US Environmental Protection Agency (EPA) publicly announced that irregularities in relation to nitrogen oxide emissions had been discovered in emission tests on certain vehicles with diesel engines, resulting in violations of US environmental laws. On 22 September 2015, the Volkswagen Group announced that around 11 million vehicles worldwide with type EA189 diesel engines were affected.

Depending on the different emissions regulations in the various countries, Volkswagen has rectified and is rectifying the diesel engine software, applied technical measures, compensated owners for reduced residual values or took back affected cars.

Volkswagen AG and the US Department of Justice, the EPA and CARB agreed that Volkswagen had to pay fines settling the majority of legal cases in the US and Canada. These fines and costs for refitting diesel cars totalled approximately EUR 23 billion. Further costs, fines and compensation for pending legal cases in other countries are evaluated and are provisioned totalling approximately EUR 9 billion.

The majority of FSNV's borrowers have either financed cars with affected diesel engines or have them in their lease car inventory. However, investors and the financial markets assess the risks FSNV

is exposed to on the background of the guarantee by FSAG, since investors have full recourse to FSAG. FSNV management has also assessed the impact of the “diesel emission issue” on the borrowers of FSNV by analysing in detail the financial situation of the borrowers as well as budget forecasts and concluded that FSNV is not exposed to higher credit risk.

Compliance with tax and regulatory requirements

The Company had its tax returns up to and including 2015 reviewed by the Dutch Tax Authorities, which resulted in an additional charge of EUR 0.7 million. For the current tax returns, a final assessment has not yet been received.

Due to its issuing activities in the capital markets and the listing at the Luxemburg Stock Exchange, the Company is complying with the regulatory requirements regarding the yearly submission of its annual financial statements to the Dutch Financial Market Authority (the “AFM”) and the approval requirements for its prospectuses by the Commission de Surveillance du Secteur Financier of the Grand Duchy of Luxembourg (the “CSSF”).

Non-financial matters

FSNV is not obliged to disclose a non-financial statement and refers to the combined, separate non-financial report of Volkswagen AG for the fiscal year 2017, which will be available on the website www.volkswagenag.com.

Expectations 2018

FSNV will continue in 2018 its issuing activities in the capital markets. In line with the long-term business strategy, the Volkswagen Financial Services Group plans to develop new markets and to improve its position in existing markets.

We expect that FSAG will keep FSNV’s capital reserve on an adequate level. As several Volkswagen Financial Services companies worldwide are going to use the attractive European funding opportunities, FSNV foresees additional requests for refinancing which will be taken care of with reinstated and increased capital market issuances under the DIP and CP-programmes.

Based on this assumption, we expect a moderate increase in total business volume for FSNV in 2018. Taking into account the expected growth in business volume and the interest environment, the development of interest income should be at a similar level as in previous years. The financial statements have been prepared under the going concern assumption.

Currently, there are no female directors on the Management or Supervisory Board. The Company will deal with this in the future.

The Management Board declares to the best of their knowledge:

1. the financial statements for 2017 give a true and fair view of the assets, the liabilities, the financial position and the results of the company; and
2. the management report gives a true and fair view of the company's situation as at the balance sheet date, the events that occurred during 2017 and the risks to which the company is exposed.

Amsterdam, 6 March 2018

Original has been signed by
Thomas Fries, Managing Director

Original has been signed by
Bernd Bode, Managing Director

Financial statements

Balance sheet as at 31 December 2017

(after proposed appropriation of profit)

	Ref.	31 December 2017		31 December 2016	
		EUR'000	EUR'000	EUR'000	EUR'000
<i>Assets</i>					
Fixed assets					
Financial fixed assets:					
Shares in participations	4	1		1	
Loans to Volkswagen Group companies	4	3,083,066		3,252,324	
Loans to joint ventures of the Volkswagen Group	4	152,570		165,071	
Total fixed assets			3,235,637		3,417,396
Current assets					
Receivables due from Volkswagen Group companies	5	2,338,480		2,816,117	
Receivables due from joint ventures of the Volkswagen Group	5	895,000		1,125,280	
Loans to external parties	6	500		500	
Other assets	7	43,679		32,339	
Prepaid and deferred charges	8	7,649		4,629	
Total current assets			3,285,308		3,978,865
Cash at banks and in hand	9		4,319		2,093
Total assets			6,525,264		7,398,354

The accompanying notes are integral parts of these financial statements.

<i>Liabilities</i>		31 December 2017		31 December 2016	
		Ref.	EUR'000	EUR'000	EUR'000
<i>Shareholder's equity and liabilities</i>					
Shareholder's equity	10				
Issued and paid-up share capital		454		454	
Share premium reserve		1,115,000		995,000	
Retained earnings		128,834		121,626	
Total shareholder's equity			1,244,288		1,117,080
Long-term liabilities					
Bonds	11	2,814,998		1,766,202	
Liabilities to Volkswagen Group companies	11	254,310		1,151,193	
Total long-term liabilities			3,069,308		2,917,395
Current liabilities					
Bonds	12	490,706		854,687	
Liabilities to Volkswagen Group companies	12	905,126		1,215,889	
Commercial papers	12	726,045		1,230,687	
Other liabilities	13	48,251		36,540	
Deferred income	14	41,540		26,076	
Total current liabilities			2,211,668		3,363,879
Total shareholder's equity and liabilities			6,525,264		7,398,354

The accompanying notes are integral parts of these financial statements.

Income statement for the year ended 31 December 2017

		2017		2016	
	Ref.	EUR'000	EUR'000	EUR'000	EUR'000
Net financial income					
Interest and similar income	16	137,588		144,784	
Interest and similar expenses	16	(126,453)		(130,379)	
Other operating income	17	1,108		1,775	
Total net financial income			12,243		16,180
Expenses					
Other operating expenses	18	(986)		(33)	
General and administrative expenses	19	(1,739)		(1,823)	
Total expenses			(2,725)		(1,856)
Result before taxation			9,518		14,324
Taxation	24		(2,310)		(4,779)
Result after taxation			7,208		9,545

The accompanying notes are integral parts of these financial statements.

Cash flow statement for the year ended 31 December 2017

	2017		2016	
	EUR'000	EUR'000	EUR'000	EUR'000
Operating profit		7,208		9,545
Adjustments for:				
Income tax expenses	(2,310)		(4,779)	
Interest and similar income	(137,588)		(144,784)	
Interest and similar expense	126,453		130,379	
		(13,445)		(19,184)
Movement in working capital				
Accrued receivables/ other assets	(14,359)		82,130	
Other liabilities	(5,765)		31,889	
Deferred income	(21,411)		(10,476)	
		(41,534)		103,543
Cash (used in) generated from operations		(47,771)		93,904
Corporate income tax paid	(2,315)		(2,328)	
Net cash used in operating activities		(50,086)		91,576
Cash flow from investment activities				
Loans issued to VW Group companies and JV	(8,814,480)		(9,444,019)	
Collection of loans to VW Group companies and JV	9,695,210		10,700,825	
Interest received	215,447		263,630	
Net cash from investment activities		1,096,177		1,520,435
Cash flow from financing activities				
Proceeds from borrowings	1,979,524		91,186	
Repayment of borrowings	(2,495,745)		(2,112,317)	
Proceeds from commercial papers	1,286,444		2,510,580	
Repayment of commercial papers	(1,790,247)		(1,791,256)	
Interest paid	(143,841)		(208,606)	
Proceeds from capital increase	120,000		(101,000)	
Net cash used in financing activities		(1,043,865)		(1,611,413)
Net cash flows		2,226		598
Balance as at 1 January		2,093		1,495
Movement		2,226		598
Balance as at 31 December		4,319		2,093

The accompanying notes are integral parts of these financial statements.

Notes to the financial statements

1 General

1.1 Activities

Volkswagen Financial Services N.V. ('FSNV' or 'the Company'), founded in 1983, is a 100% subsidiary of Volkswagen Financial Services AG ('FSAG'), who in turn is a 100% subsidiary of Volkswagen AG ('VWAG').

FSNV's registered office is located at Paleisstraat 1, 1012 RB Amsterdam, The Netherlands. The Company is registered with the Dutch Register of Commerce under No. 33172400. FSNV maintains a website at www.vwfs.nl.

The main purpose of the Company is the financing of and participation in Group companies. FSNV has access to several funding sources such as bonds, notes and commercial paper as well as inter-company loans.

All external issuances of financial instruments are guaranteed by FSAG. FSNV has lent more than 95% of the proceeds of these borrowings to Group companies or joint ventures.

Due to its issuing activity in the capital markets, FSNV is subject to the regulatory supervision by the Dutch Financial Market Authority (Autoriteit Financiële Markten, 'AFM') and has to submit its yearly and half-yearly annual reports to the AFM.

Bonds issued by FSNV are listed at the Luxemburg Stock Exchange. The bond prospectuses have been approved by the Commission de Surveillance du Secteur Financier of the Grand Duchy of Luxembourg ('CSSF').

1.2 Provisions

Provisions are recognised for legally enforceable or constructive obligations that exist at the balance sheet date, and for which it is probable that an outflow of resources will be required and a reliable estimate can be made.

Provisions are measured at the best estimate of the amount that is necessary to settle the obligation as per the balance sheet date. Provisions for pension are valued on the basis of actuarial principles. The other provisions are carried at the nominal value of the expenditure that is expected to be necessary in order to settle the obligation, unless stated otherwise.

If obligations are expected to be reimbursed by a third party, such reimbursement is included as an asset in the balance sheet if it is probable that such reimbursement will be received when the obligation is settled.

1.3 Related parties

All legal entities that can be controlled, jointly controlled or significantly influenced by FSNV are considered to be related parties. Also entities which can control or significantly influence the Company are considered to be related parties. In addition, statutory directors, other key management of the Company or the ultimate parent company and close relatives are regarded as related parties.

1.4 Consolidation and shares in participations

FSNV holds one share in VW Finance Belgium SA, Brussels, Belgium with a cost price of EUR 500. The issued share is less than 20% of the total shares of VW Finance Belgium SA. The parent company of FSNV is FSAG (Brunswick, Germany). The consolidation, including all subsidiaries of FSNV, is performed at FSAG level. These consolidated financial statements can be obtained from the Company.

1.5 Note to the cash-flow statement

Consolidated cash flows for the whole Volkswagen Financial Services Group are included in the Volkswagen AG consolidated financial statements; therefore a separate cash flow statement for the Company is not required by Dutch law. To be in line with practice in the capital market, FSNV prepares a cash flow statement, using the indirect method.

The cash items disclosed in the cash flow statement are comprised of cash and cash equivalents. Cash flows denominated in foreign currencies have been translated at average exchange rates. Exchange differences affecting cash items are included in the respective amounts.

Cash from loans granted and interest received are included in cash from/ used in investment activities. Cash from borrowings, including interest paid and capital increases/ dividends paid/ received are included in cash from/ used in financing activities.

All other movements are included in cash used/ generated from operations.

1.6 Estimates

The preparation of financial statements in conformity with the relevant rules requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. If necessary for the purposes of providing the view required under Section 362(1), Book 2, of the Dutch Civil Code, the nature of these estimates and judgements, including the related assumptions, is disclosed in the notes to the financial statement items in question. Estimates used for accounting of financial fixed assets and impairment of loans granted are disclosed under note 2.6 and 2.11

2 Principles of valuation of assets and liabilities

2.1 General

The financial statements are prepared in accordance with the statutory provisions of Part 9, Book 2 of the Dutch Civil Code and the firm pronouncements in the Guidelines for Annual Reporting in the Netherlands as issued by the Dutch Accounting Standards Board. The financial statements are presented in EUR, which is also the Company's functional currency, and have been prepared on a going concern basis.

In general, assets and liabilities are stated at the amounts at which they were acquired or incurred, or fair value. If not specifically stated otherwise, they are recognised at the amounts at which they were acquired or incurred. The balance sheet and the income statement include references to the notes.

Unless otherwise stated, amounts are shown in thousands of euros (EUR'000). All amounts shown are rounded, so minor discrepancies may arise from addition of these amounts. Negligible discrepancies could also arise in the comparison with the prior year owing to adjustments in the rounding methodology.

2.2 *Comparison with prior year*

The principles of valuation and determination of result remain unchanged compared to the prior year.

2.3 *Foreign currencies*

Functional currency

Items in the financial statements of the Company's borrowers and subsidiaries are stated with due observance of the currency of the primary economic environment in which the respective group company operates (the functional currency). The financial statements are presented in EUR, i.e. the functional and reporting currency of FSNV.

Transactions, receivables and liabilities

Monetary assets and liabilities denominated in foreign currencies are translated at the period end-rate prevailing on the balance sheet date. Investments in participations are stated at the historical exchange rate at the date of the transaction.

Transactions denominated in foreign currencies in the reporting year are recognised in the financial statements at the exchange rate ruling at the transaction date.

In respect of any positions in the balance sheet that are covered by cross currency interest rate swaps or by foreign exchange forward contracts, the differences in values calculated at closing rates at the end of the year and contract rates are allocated to the respective principals of the loans. If the loan taken is denominated in a currency other than EUR, the respective correction is allocated to this loan. Otherwise, the corresponding loan granted is corrected.

Hedge accounting

FSNV applies hedge accounting. Relationships between hedging instruments and hedged items are documented at the inception of the transaction. FSNV also assesses, both at hedge inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. This is done by comparing the critical qualitative characteristics of the hedge instrument with those of the hedged position. If there is an indication of ineffectiveness, the Company measures this potentially ineffective part by conducting a quantitative ineffectiveness analysis.

2.4 *Intangible fixed assets*

Intangible fixed assets are carried at historical cost less amortisation. Any impairment as at the balance sheet date is taken into account; impairment exists if the carrying amount of the asset (or the cash-generating unit to which it belongs) exceeds its recoverable amount.

Software licences acquired are capitalised at acquisition cost and amortised over the estimated economic life of three years. Expenditures incurred for the production of identifiable software products that are tailor-made for the group are capitalised. Expenditure in connection with maintenance of computer software and expenses related to research activities are recognised in the income statement.

The useful economic life and amortisation method is evaluated as per each balance sheet date.

2.5 *Tangible fixed assets*

Fixed assets are valued at acquisition or production cost including directly attributable expenses, less straight-line depreciation over the estimated useful economic life, or market value if lower. Directly attributable production costs include the costs of the raw materials and consumables, and also include installation costs.

For computer hardware a depreciation period of 3 years is used.

The useful economic life and depreciation method is evaluated as of each balance sheet date.

2.6 *Financial fixed assets*

Shares in participations

The investment in the group company is a minority interest and as the Company cannot exercise significant influence, the asset is stated at acquisition price.

The share in the group company is specified in note 1.4.

Loans to Volkswagen Group companies and joint ventures of the Volkswagen Group and to third parties

These loans to Volkswagen Group companies, other participating interests and third parties are loans with a remaining term of more than one year. Receivables disclosed under financial fixed assets are recognised initially at fair value of the amount owed. These receivables are subsequently measured at amortised cost. The main rule is that amortised cost equals the carrying amount of the asset net of any repayments on the principal and plus, or net of, the accumulated amortisation, calculated using the effective interest method, of the difference between the amount upon initial recognition (including transaction costs) and the repayments. Straight-line amortisation in determining amortised cost is allowed as an alternative if straight-line amortisation does not lead to significant discrepancies with the effective interest method. If loans are issued at a discount or premium, the discount or premium is recognised through profit or loss over the maturities of the loans using the effective interest method. Also transaction costs are included in the initial valuation and recognised in profit or loss as part of the effective interest method. Impairment losses are deducted from amortised cost and expensed in the income statement.

Receivables from joint ventures of the Volkswagen Group

Interest receivables from joint ventures of the Volkswagen Group are receivables with a remaining term of more than one year and are valued at their nominal value.

2.7 *Current assets*

All current assets have a maturity within one year.

Receivables due from Volkswagen Group companies and joint ventures of the Volkswagen Group

Receivables are recognised initially at fair value and subsequently measured at amortised cost.

Other assets

The swap interest receivables and income tax receivables are shown under other assets and are initially valued at cost and subsequently at their amortised cost value.

Prepaid and deferred charges

Prepaid and deferred charges are initially valued at cost and are amortised over the remaining life of the services or of the bonds.

Cash at banks and in hand

Cash at banks and in hand represents cash in hand and bank balances. Cash at banks and in hand is carried at nominal value. Cash at banks denominated in foreign currencies are translated at the period end-rate prevailing on the balance sheet date.

2.8 Long-term liabilities

Bonds

The bonds are initially valued at fair value with subsequent measurement at their amortised cost value. All long-term bonds have a remaining maturity of more than one year. No assets were pledged as collateral by the Company.

Liabilities to Volkswagen Group companies

The liabilities to Volkswagen Group companies are initially valued at fair value with subsequent measurement at their amortised cost value. All liabilities have a maturity of more than one year.

2.9 Current liabilities

Bonds

The bonds are initially valued at fair value with subsequent measurement valued at their amortised cost value. All short-term bonds are payable within one year.

Commercial papers

The commercial papers are initially valued at fair value with subsequent measurement valued at their amortised cost value.

Liabilities to Volkswagen Group companies

The liabilities to affiliated companies are initially valued at fair value with subsequent measurement valued at their amortised cost value. All liabilities are payable within one year.

Other liabilities

The swap interest payables with a run-off period within one year are shown under other liabilities and are valued at their nominal value.

Trade payables

The trade payables are initially valued at fair value and subsequently at their amortised cost value and are payable within one year.

Other accrued liabilities

The accruals are based on sound business judgement and valued at the expected costs.

Deferred income

The deferred income concerns premiums and cost compensations and is amortised over the remaining life of the loans taken.

Deferred income tax

Deferred tax liabilities are recognised to provide for timing differences between the value of the assets and liabilities for financial reporting purposes on the one hand and for tax purposes on the other. Deferred tax liabilities are calculated based on the tax rate prevailing on the balance sheet date or the rates that will apply in the future, insofar as these have been set down by law.

Current income tax

The current Dutch nominal tax rate of 25% has been applied.

2.10 Financial instruments

Loans included in financial and current assets, as well as liabilities and derivative financial instruments, are stated at amortised cost. The Company applies hedge accounting to hedging instruments when hedging interest and currency risk on borrowings and lendings. The Company documents the relationship between hedging instruments and hedged items at the inception of the transaction. Both the derivative and the hedged item are stated at amortised cost. The gain or loss relating to any ineffective portion is recognised in the income statement within finance cost. For more information about the value of the assets, assigned as hedged item, see note 4 and 5, of the liabilities see notes 11 and 12 and of the financial instruments see note 23. The Company has no derivative financial instruments other than the ones used for hedging.

Cost price hedge accounting

The Company applies cost price hedge accounting to hedge interest risk and FX-risk on borrowings.

In applying cost price hedge accounting, the initial recognition of, and the accounting policies for, the hedging instrument are dependent on the hedged item, which has the following implications:

- if the hedged item is recognised at cost in the balance sheet, the derivative instrument is also stated at cost;
- as long as the hedged item is not yet recognised in the balance sheet, the hedging instrument is not re-measured (this applies, for instance, to hedging currency risks on future transactions);
- if the hedged item qualifies as a monetary item denominated in a foreign currency, the derivative instrument, where it has currency elements, is also stated at the period end-rate prevailing at the balance sheet date.

The ineffective portion of the hedge is recognised directly in the income statement.

Hedge effectiveness is assessed by comparing the critical characteristics of the hedge instrument with those of the hedged position. If there is an indication of ineffectiveness, the Company measures this potentially ineffective part by conducting a quantitative ineffectiveness analysis.

2.11 Impairment of financial assets

On each balance sheet date, the Company tests whether there are any indications of assets being subject to impairment. If any such indications are present, the recoverable amount of the asset is determined. If this proves to be impossible, the recoverable amount of the cash-generating unit to which the asset belongs is determined. An asset is subject to impairment if its carrying amount is higher than its realisable value; the realisable value is the higher of the fair value less costs to sell and the value in use.

The fair value is determined based on the active market. Impairment is directly recognised as an expense in the income statement.

If it is established that a previously recognised impairment no longer applies or has declined, the increased carrying amount of the assets in question is not set higher than the carrying amount that would have been determined had no asset impairment been recognised.

The value of an asset in use is determined by estimation of the future net cash flows, based on continued use of the asset.

2.12 General

Result is determined as the difference between the realisable value of services rendered and the costs and other charges for the year. Results on transactions are recognised in the year in which they are realised; losses are taken as soon as they are foreseeable.

2.13 Revenue recognition

Revenue from interest income is allocated to the reporting year in which it occurs. Exchange rate differences arising upon the settlement of monetary items are recognised in the income statement in the period that they arise.

2.14 Exchange rate differences

Exchange rate differences arising upon the settlement of monetary items are recognised in the income statement in the year that they arise unless hedged (notes 17 and 18).

2.15 Interest income and similar income and interest expenses and similar expenses

Interest income and expenses are recognised on a pro-rata basis, taking into account the effective interest rate of the assets and liabilities concerned. When recognising the interest charges, the transaction cost on the loans received is taken into account.

2.16 Other operating income and expenses

Other operating income and expenses include income and expenses that are not directly attributable to the interest income and expenses.

2.17 General and administrative expenses

These expenses include expenses such as personnel expenses, office expenses, consulting and audit fees and depreciation and amortisation.

Depreciation

Intangible fixed assets are amortised and tangible fixed assets are depreciated over their expected useful lives as from the inception of their use. Future depreciation is adjusted if there is a change in estimated useful life.

Gains and losses upon the sale of tangible fixed assets are included in other operating income or other operating expenses respectively.

Labour and other costs

Services performed by Volkswagen International Finance N.V. ('VIF') for FSNV are charged at a fixed amount. The fixed amount is evaluated in regular intervals. These costs include for example salaries, rental costs and general costs.

2.18 Taxation

Profit tax is calculated on the profit before taxation in the income statement, taking into account any losses carried forward from previous financial years (insofar as these are not included in deferred tax assets), tax-exempt items and non-deductible expenses. Account is also taken of changes in deferred tax assets and deferred tax liabilities owing to changes in the applicable tax rates.

3 Financial instruments and risks

3.1 Market risk

General market risk due to events at Volkswagen AG

Government authorities in a number of jurisdictions worldwide have conducted and are conducting investigations of Volkswagen Group regarding findings of irregularities in relation to exhaust emissions from diesel engines in certain Volkswagen Group vehicles. The results of these and any future investigations and criminal litigations, may have a material adverse effect on Volkswagen Group's business, financial position, results of operations and reputation, as well as the prices of its securities and its ability to make payments under its securities.

Volkswagen Financial Services N.V.'s commercial success largely depends on the financial health and the reputation of the ultimate shareholder Volkswagen AG and due to the events, Volkswagen Financial Services N.V. may not succeed in obtaining funds for financing requests in due time and to the extent necessary.

In addition, because of the investigations, Volkswagen Financial Services N.V. as an issuer may face risks arising from legal disputes with investors claiming damages for alleged breaches of capital market laws.

Currency risk

To avoid currency risk, the loans to FSAG group companies and to joint ventures of the FSAG Group and the related funding are generally matched in currency terms. If not, currency swaps are executed to achieve the matched basis.

In cases where the matching cannot be achieved completely, the Supervisory Board has set small currency limits for individual currencies. Matching policies are closely monitored and enforced. Consequently, currency risk is comparatively remote. In 2017, the limits were not exceeded.

Interest rate risk

Based on funding requests by FSAG group companies and joint ventures of the FSAG Group FSNV issues notes to investors matching the fixed or variable interest requirement of the FS related parties. In cases where the investor looks for a different interest structure, FSNV is using interest rate swaps or cross currency interest rate swaps to convert the interest into the structure required by the related parties. The Supervisory Board authorised FSNV to run a certain interest rate risk. A limit system and tools to monitor and manage the risk have been set up. Interest mismatches are permitted within a twelve-month period only. Therefore, the risk is comparatively low. In 2017, no limits were exceeded.

3.2 Credit risk

The risk of default arising from loans granted, account balances and derivative financial instruments involves the risk of default by counterparties.

FSNV is extending loans to FSAG group companies and to joint ventures of FSAG Group, which are granted according to the guidelines and instructions from FSAG, the guarantor of commercial paper and capital market issuances by FSNV. The default risk of FSNV-borrowers has been analysed based on financial reports, planning forecasts and discussions with FSAG headquarters. Based on the analysis, the credit risk of FSNV-borrowers is considered to be remote.

For FSNV's external bank counterparties risk is limited by a limit system centrally managed by FSAG Group Risk Management taking into account also the credit assessments by the international rating agencies. Credit risk with external counterparties materialises from account balances, deposits and derivative transactions with a positive fair value. Given the business purpose of FSNV, account balances and deposits are zero or kept to a minimum. Regarding the derivative transactions, exposure is kept within the risk limits defined by FSAG Group Risk Management.

3.3 *Liquidity risk*

Based on funding requests by FSAG related parties, FSNV issues commercial paper and bonds to investors. Funds taken from investors are extended with the same maturity to FSAG-Group borrowers.

In cases where this matching cannot be achieved the Supervisory Board has set narrow liquidity risk limits. The Company monitors the limits on a permanent basis. Against the background of the relatively narrow limits and the strong financial solidity of the Volkswagen Group, the liquidity risk is remote. In 2017, no limits were exceeded. Notes issued by FSNV have the benefit of a Guarantee and Negative Pledge (The Guarantee) given by Volkswagen Financial Services AG (The Guarantor).

The Debt Issuance Program under which FSNV is issuing bonds, is regularly updated to incorporate current developments. FSNV also continues to issue Commercial Papers based on the existing EUR 5 billion Commercial Paper Program to finance the requirements of FSAG group companies and joint ventures of FSAG group

Based on the diversified funding strategy, Volkswagen Financial Service AG acted flexibly to refinance its activities with the increased issuance of secured bonds (ABS), direct bank deposits and bank credit facilities.

4 **Financial fixed assets**

Shares in participations

The Company's interests in other companies consists of 1 share in VW Finance Belgium S.A. located in Brussels, Belgium which represents less than 5% of the total equity of the entity. The carrying amount is EUR 500 as at 31 December 2017 (2016: EUR 500). There was no movement in the account balance in both years. The Company has not identified any indicator of impairment in 2017 (2016: nil).

Loans to Volkswagen Group companies and joint ventures of the Volkswagen Group included in financial fixed assets

The breakdown of the loans to Volkswagen Group companies and joint ventures of the Volkswagen Group is as follows:

	Original currency	Weighted average interest rate (%)	31 December 2017	
			Book value	Market value
			EUR'000	EUR'000
Fixed asset loans to Volkswagen Group companies	GBP	1,4197	2,477,766	2,500,942
	EUR	0,3398	319,310	319,922
	KRW	3,3467	100,000	102,774
	SEK	0,1410	153,933	153,603
	CZK	0,9450	32,057	32,174
			3,083,066	3,109,415
Fixed asset loans to joint ventures of the Volkswagen Group	NOK	1,6683	152,570	153,803
Total loans to Volkswagen Group companies and joint ventures of the Volkswagen Group			3,235,636	3,263,218

The market values are determined based on discounted cash flows. Specific credit spreads per counterparty were not included in the model used to determine the market value. Since all loans are to Volkswagen Group companies and joint ventures, the credit spread applicable to these loans is equal to the credit spread for the Volkswagen Group.

As at December 31, the following credit spreads were applicable:	2017	2016
	BPS	BPS
For amounts payable within one year:	15,08	21,83
For amounts payable between one year and five years:	27,00	57,75
For amounts payable after five years	70,20	105,20

For comparison, the fixed asset loans overview of 2016:

	Original currency	Weighted average interest rate (%)	31 December 2016	
			Book value	Market value
			EUR'000	EUR'000
Fixed asset loans to Volkswagen Group companies	GBP	1,1716	1,570,788	1,563,585
	EUR	0,1651	1,123,972	1,122,953
	KRW	2,7824	280,000	292,325
	AUD	3,4333	220,000	217,860
	CZK	0,5616	57,564	57,915
			3,252,324	3,254,638
Fixed asset loans to joint ventures	NOK	1,5960	165,071	166,056
Total loans to Volkswagen Group companies and joint ventures of the Volkswagen Group			3,417,395	3,420,694

5 Receivables due from Volkswagen Group companies and joint ventures of the Volkswagen Group

	Original currency	Weighted average interest rate (%)	31 December 2017	
			Book value	Market value
			EUR'000	EUR'000
Current receivables due from Volkswagen Group companies	EUR	0,0586	1,137,952	1,153,743
	GBP	1,2518	338,104	337,943
	AUD	3,1013	530,000	513,694
	CZK	0,1598	140,358	141,216
	KRW	2,4700	180,000	183,277
Accrued interest and other receivables			12,066	12,066
			<u>2,338,480</u>	<u>2,341,939</u>
Current receivables due from joint ventures of the Volkswagen Group	TRY	13,5451	615,061	559,899
	NOK	1,2757	152,602	152,654
	EUR	0,3536	93,996	94,101
Accrued interest and other receivables			33,341	33,341
			<u>895,000</u>	<u>839,995</u>
Total receivables due from Volkswagen Group companies and joint ventures			<u>3,233,480</u>	<u>3,181,934</u>

For the determination of the market values, see note 4.

As mentioned in note 2.11, the terms of all outstanding loans to Volkswagen Group companies and joint ventures are hedged, using derivatives to match the terms of the bonds and loans from Volkswagen Group companies, used to fund the financing requirements of Volkswagen Group companies and joint ventures. As a result, the Company has principally no exposure to interest rate risk and currency risk.

For comparison, the overview of 2016:

	Original currency	Weighted average interest rate (%)	31 December 2016	
			Book value	Market value
			EUR'000	EUR'000
Current receivables due from Volkswagen Group companies excluding interest	EUR	0,3435	1,392,619	1,394,674
	GBP	1,4137	525,062	507,421
	AUD	2,9249	310,000	307,106
	SEK	0,3704	290,840	291,331
	CZK	0,0807	164,810	164,274
	KRW	2,7644	70,000	75,756
	PLN	0,8075	50,000	48,926
Accrued and other receivables			12,786	12,786
			2,816,117	2,802,274
Current receivables due from joint ventures of the Volkswagen Group excluding interest	TRY	10,4545	643,618	568,772
	NOK	1,6193	274,992	276,535
	EUR	0,5281	182,391	182,707
Accrued and other receivables			24,279	24,279
			1,125,280	1,052,293
Total receivables due from Volkswagen Group companies and joint ventures of the Volkswagen Group			3,941,397	3,854,567

6 Loans to external parties

This balance sheet position contains loans to external parties:

Company	Original currency	Interest rate	Amount In EUR	Maturity
Pon Auto Import Nederland B.V., Leusden	EUR	0,800	100,000	25-05-2018
Pon Automotive B.V., Leusden	EUR	0,800	200,000	25-05-2018
Pon Holdings B.V., Almere	EUR	0,800	200,000	25-05-2018

These Dutch companies do not belong to the Volkswagen Group. The loans are not guaranteed by FSAG. The fair values of these loans approximate their carrying value.

The interest rates charged on the above loans are calculated on 1-year Euribor plus a margin based on market price margin for investment graded companies.

For comparison, the overview of loans to external parties as at 31 December 2016:

Company	Original currency	Interest rate	Amount In EUR	Maturity
Pon Auto Import Nederland B.V., Leusden	EUR	1,162	100,000	25-05-2017
Pon Automotive B.V., Leusden	EUR	1,162	200,000	25-05-2017
Pon Holdings B.V., Almere	EUR	1,162	200,000	25-05-2017

7 Other assets

This account consists of the following:

	31 Dec 2017	31 Dec 2016
	EUR'000	EUR'000
Interest receivables from banks arising from derivatives	38,032	26,128
Income tax receivable	5,385	1,371
Unrealized FX gains and losses	262	4,839
Other debtors	-	1
	<u>43,679</u>	<u>32,339</u>

The income tax receivable relates to recoverable income and withholding taxes.

8 Prepaid and deferred charges

	31 Dec 2017	31 Dec 2016
	EUR'000	EUR'000
Prepaid and deferred charges	7,649	4,629
	<u>7,649</u>	<u>4,629</u>

The prepaid and deferred charges mainly consist of deferred emission costs. The deferrals arise from capitalised issuance expenses, which will be amortised during the term of the regarding bond.

9 Cash at banks and in hand

	31 Dec 2017	31 Dec 2016
	EUR'000	EUR'000
Cash at Volkswagen Bank account	4,071	1,412
Cash at external bank accounts	248	681
	<u>4,319</u>	<u>2,093</u>

All cash balances are at the free disposal of the Company and bear market interest rates. The credit risk for cash at external bank accounts is based on a risk assessment and within the limits defined by FSAG Group Risk Management.

10 Shareholder's equity

	<i>Issued and paid-up share capital</i>	<i>Share premium reserve</i>	<i>Retained earnings</i>	<i>Total equity</i>
	EUR'000	EUR'000	EUR'000	EUR'000
Balance as at 1 January 2016	454	1,096,000	112,081	1,208,535
Contribution from FSAG	-	400,000	-	400,000
Repayment of contribution to FSAG	-	(501,000)	-	(501,000)
Result for the year 2016	-	-	9,545	9,545
Balance as at 31 December 2016	<u>454</u>	<u>995,000</u>	<u>121,626</u>	<u>1,117,080</u>
Balance as at 1 January 2017	454	995,000	121,626	1,117,080
Contribution from FSAG	-	120,000	-	120,000
Result for the year 2017	-	-	7,208	7,208
Balance as at 31 December 2017	<u>454</u>	<u>1,115,000</u>	<u>128,834</u>	<u>1,244,288</u>

The shareholder's equity consists of the following:

Share capital

On 31 December 2017, the subscribed capital of the Company amounted to EUR 2.3 million, of which an amount of EUR 454,000 was paid-up, representing 454 registered and issued shares of EUR 1,000 each. The Company has no mandatory statutory reserve.

Share premium reserve

To increase flexibility in group financing, an amount of EUR 120.0 million was newly contributed by FSAG in 2017. The contribution from FSAG and repayment of contribution to FSAG amounted to EUR 400.0 million and EUR 501.0 million, respectively in 2016. The balance of the share premium reserve at the end of 2017 amounted to EUR 1.1 billion (2016: EUR 995.0 million).

Retained earnings

At the end of 2017, the total retained earnings amounted to EUR 128.8 million (2016: EUR 121.6 million) and the total equity amounted to EUR 1.2 billion (2016: EUR 1.1 billion).

11 Long-term liabilities

	31 Dec 2017	31 Dec 2016
	EUR'000	EUR'000
Bonds listed	1,972,174	1,134,504
Bonds unlisted	842,824	631,698
	<u>2,814,998</u>	<u>1,766,202</u>

The breakdown of the long-term bonds is as follows:

	Original currency	Average interest rate as percentage	31 December 2017	
			Book value	Market value
			EUR'000	EUR'000
Maturity longer than 5 years				
Bonds listed	GBP	2,2500	394,455	396,581
Maturity less than 5 years				
Bonds listed	GBP	2,2857	1,183,365	1,204,075
Bonds listed	NOK	1,4625	152,602	153,956
Bonds listed	SEK	4,2500	152,572	152,165
Bonds listed	NZD	0,6300	57,122	60,628
Bonds listed	CZK	2,6250	32,058	32,058
Bonds unlisted	GBP	2,8125	732,560	738,962
Bonds unlisted	NZD	1,1250	110,264	120,774
Total long-term bonds			<u>2,814,998</u>	<u>2,859,199</u>

For comparison purposes, the overview of long-term bonds as at 31 December 2016 is as follows:

	Original currency	Average interest rate as percentage	31 December 2016	
			Book value	Market value
			EUR'000	EUR'000
Maturity less than 5 years				
Bonds listed	GBP	2,5735	990,099	1,024,602
Bonds listed	NZD	4,8750	59,038	67,329
Bonds listed	NOK	1,3750	55,024	55,105
Bonds listed	CZK	0,6300	30,343	30,328
Bonds unlisted	GBP	1,7500	407,687	412,927
Bonds unlisted	NZD	4,2500	113,963	132,753
Bonds unlisted	NOK	1,2500	110,048	109,833
Total long-term bonds			1,766,202	1,832,877

The bonds are issued under the existing EUR 25bn DIP Programme and rank pari passu with the existing issuance.

Liabilities to Volkswagen Group companies excluding interest

A breakdown of the long-term liabilities to Volkswagen Group companies is as follows:

	Original currency	Average interest rate as percentage	31 December 2017	
			Book value	Market value
			EUR'000	EUR'000
Maturity less than 5 years				
VWGoAF	USD	2,3270	254,310	290,231
			254,310	290,231

For comparison purposes, the overview of 2016 is as follows:

31 December 2016				
	Original currency	Average interest rate as percentage	Book value	Market value
			EUR'000	EUR'000
Maturity less than 5 years				
VWGoAF	USD	2,0025	1,151,193	1,287,843
			<u>1,151,193</u>	<u>1,287,843</u>

The credit ratings of the rating agencies are derived from FSAG's rating:

2017			
Agency	Short-term	Long term	Outlook
Moody's	Prime-2	A-3	Negative
Standard & Poor's	A-2	BBB+	stable
2016			
Agency	Short-term	Long term	Outlook
Moody's	Prime-1	A-2	Negative
Standard & Poor's	A-2	BBB+	Watch negative

12 Current liabilities

	31 Dec 2017	31 Dec 2016
	EUR'000	EUR'000
Bonds listed	388,972	750,163
Bonds unlisted	101,734	104,524
	<u>490,706</u>	<u>854,687</u>

The breakdown of the current bonds is as follows:

	Original currency	Average interest rate as percentage	31 December 2017	
			Book value	Market value
			EUR'000	EUR'000
Maturity less than 1 year				
Bonds listed	GBP	2,7500	338,104	342,158
Bonds listed	NOK	1,1250	50,867	51,015
Bonds unlisted	NOK	2,1875	101,735	101,784
Total current bonds			490,706	494,957

For comparison purposes, the overview of current bonds as at 31 December 2016 is as follows:

	Original currency	Average interest rate as percentage	31 December 2016	
			Book value	Market value
			EUR'000	EUR'000
Maturity less than 1 year				
Bonds listed	EUR	0,0000	60,000	60,000
Bonds listed	SEK	0,0000	156,786	156,745
Bonds listed	GBP	1,7500	291,206	291,238
Bonds listed	NOK	2,1667	165,071	165,581
Bonds listed	CAD	2,1250	77,101	70,422
Bonds unlisted	SEK	0,4070	104,523	104,707
Total current bonds			854,687	848,693

Liabilities to Volkswagen Group companies

The breakdown of the current liabilities, including accrued interest to Volkswagen Group companies is as follows:

	Original currency	Average interest rate as percentage	31 December 2017	
			Book value	Market value
			EUR'000	EUR'000
Volkswagen FSAG	EUR	0,000	20,000	20,002
VWGoAF	USD	1,8890	882,710	830,977
Accrued interest	EUR		2,416	-
			905,126	850,979

For comparison purposes, the overview of current liabilities, including accrued interest to Volkswagen Group companies as at 31 December 2016 is as follows:

	Original currency	Average interest rate as percentage	31 December 2016	
			Book value	Market value
			EUR'000	EUR'000
VWGoAF	USD	1,4660	910,390	1,182,866
Skoda	CZK	0,3643	300,427	307,502
Accrued interest	EUR		5,072	5,072
			<u>1,215,889</u>	<u>1,495,440</u>

Commercial papers

A breakdown of the current liabilities from issued commercial paper as per 31 December 2017 is as follows:

	Original currency	Average interest rate as percentage	31 December 2017	
			Book value	Market value
			EUR'000	EUR'000
Average term 6 months				
Commercial Papers	EUR	-0,041	726,045	725,762
Total commercial papers			<u>726,045</u>	<u>725,762</u>

For comparison the overview of 2016:

	Original currency	Average interest rate as percentage	31 December 2016	
			Book value	Market value
			EUR'000	EUR'000
Average term 8 months				
Commercial Papers	EUR	0,2054	1,179,471	1,178,669
Commercial Papers	SEK	0,0957	51,216	51,249
Total commercial papers			<u>1,230,687</u>	<u>1,229,918</u>

13 Other liabilities

	<u>31 Dec 2017</u>	<u>31 Dec 2016</u>
This account consists of the following:	EUR'000	EUR'000
Loan interest payable	35,302	24,187
Unrealized FX gains and losses	8,079	2,132
Swap interest payable	2,806	8,048
Current income tax	1,352	1,443
Withholding tax payable	571	650
Accrued liabilities	141	59
Accounts payable	-	21
	<u>48,251</u>	<u>36,540</u>

14 Deferred income

	<u>31 Dec 2017</u>	<u>31 Dec 2016</u>
	EUR'000	EUR'000
Capitalised issue income	41,540	26,076
	<u>41,540</u>	<u>26,076</u>

Capitalised issue income relates to received up-front payments from cross-currency interest rate swaps, compensating the emission costs incurred on bonds.

15 Commitments not included in the balance sheet

The following revolving credit facilities are currently outstanding:

Borrower	Currency	Amount in EUR'000	Effective date	Termination date
LLC VW Bank Rus	RUB	8,000,000	20.02.2012	Open
VW Group Finanz OOO	RUB	2,300,000	10.12.2007	Open
SkoFIN	CZK	4,000,000	03.09.2012	Open
MAN Financial Services OOO	RUB	3,000,000	02.07.2015	Open
VW Financial Services Russia LLC	RUB	8,000,000	02.07.2015	Open

For comparison, the overview of outstanding revolving credit facilities as at 31 December 2016:

Borrower	Currency	Amount in EUR'000	Effective date	Termination date
LLC VW Bank Rus	RUB	8,000,000	20.02.2012	Open
VW Group Finanz OOO	RUB	2,300,000	10.12.2007	Open
SkoFIN	CZK	4,000,000	03.09.2012	Open
MAN Financial Services OOO	RUB	3,000,000	02.07.2015	Open
VW Financial Services Russia LLC	RUB	8,000,000	02.07.2015	Open

16 Financial income and expenses

	2017	2016
	EUR'000	EUR'000
Interest and similar income	137,588	144,784
Interest and similar expenses	126,453	130,379
	<u>11,135</u>	<u>14,405</u>

17 Other operating income

	2017	2016
	EUR'000	EUR'000
Miscellaneous income previous years	1,108	4
Exchange result	-	1,771
	<u>1,108</u>	<u>1,775</u>

The miscellaneous income previous years relate to withholding taxes.

18 Other operating expenses

	2017	2016
	EUR'000	EUR'000
Miscellaneous expenses previous years	970	33
Bank charges	16	-
	<u>986</u>	<u>33</u>

The miscellaneous expenses previous year relate to withholding taxes.

19 General and administrative expenses

	2017	2016
	EUR'000	EUR'000
Personnel and other third party costs	1,344	1,450
Consulting and auditing fees	135	95
Electronic Data Processing expenses	188	198
General office expenses	54	59
Directors' and Officers' liability insurance	18	21
	<u>1,739</u>	<u>1,823</u>

The personnel and other third party costs is a charge from VIF for services rendered to FSNV. Due to a re-negotiation of the Service Level Agreement in January 2015, the amount charged for these services will fluctuate on a year-to-year basis.

20 Independent auditor's fees

The following fees based on invoices and estimated work orders for assurance services incurred in the reporting year:

	2017	2016
	EUR'000	EUR'000
Audit of the financial statements	47	35
Other audit procedures	31	31
Tax services	-	-
Other non-audit services	-	-
	78	66

The audits of the statutory accounts in 2017 and in 2016 were performed by BDO Audit & Assurance B.V.

The other audit procedures relate to the audit of the group reporting packages and were performed by PricewaterhouseCoopers Accountants N.V.

No tax services nor other non-audit services were rendered by either PricewaterhouseCoopers Accountants N.V. or BDO Audit & Assurance B.V.

21 Related parties

Related party transactions include:

All loans granted to Volkswagen Group companies and Joint Ventures of Volkswagen Group, including the corresponding interest- and similar income, with exception for the loans mentioned in note 6.

For receivables due from Volkswagen Group companies, see note 4 and 5.

For liabilities to Volkswagen Group companies, see note 11 and 12.

For cash at Volkswagen Bank account, see note 9.

22 Average number of employees

The employees are supplied by VIF. The costs regarding the work performed for FSNV are included in the service charges of EUR 1.3 million, which are included in the general and administrative expenses.

23 Financial instruments

The Company's policy is to fully hedge its interest rate and exchange rate exposures. The current hedges are all 100% effective.

The financial instruments of the Company had the following notional amounts:

	Interest swaps	Interest/ currency swaps	FX Contracts	Total
	EUR'000	EUR'000	EUR'000	EUR'000
31 December 2017	2,918,081	1,807,712	1,044,522	5,770,315
31 December 2016	2,019,134	3,279,022	1,374,660	6,672,816

The financial instruments of the Company had the following positive or negative market values:

	Interest swaps	Interest/ currency swaps	FX contracts	Total
	EUR'000	EUR'000	EUR'000	EUR'000
31 December 2017				
Positive market value	32,473	71,571	29,980	134,024
Negative fair value	(3,697)	(73,592)	(9,017)	(86,306)
Total market value	28,776	(2,021)	20,963	47,718
31 December 2016				
Positive market value	56,407	417,378	64,652	538,438
Negative fair value	-	(17,596)	(3,451)	(21,047)
Total market value	56,407	399,782	61,202	517,391

24 Taxation

The taxation on the result on ordinary activities can be specified as follows:

	2017	2016
	EUR'000	EUR'000
Result before taxation	9,518	14,324
Taxation on result	2,310	4,779
Effective tax rate	24.3%	33.4%
Applicable tax rate	25.0%	25.0%

25 Profit distribution

Management proposes to retain the 2017 profit of EUR 7,207,940.26.

26 Post balance sheet events

No post balance sheet events that require disclosure nor adjustment have occurred.

27 Members of Management Board and Supervisory Board

Management Board:

- Thomas Fries, Amsterdam
- Bernd Bode, Hannover

Supervisory Board:

- Frank Fiedler, Braunschweig

The members of Management Board and Supervisory Board have not received any remuneration for 2017 in their capacities as Directors of the Company (2016: nil).

Amsterdam, 6 March 2018

Management Board,

Supervisory Board,

Original has been signed by
T. Fries

Original has been signed by
F. Fiedler

Original has been signed by
B. Bode

Other information

Profit appropriation according to the Articles of Association

The Company's Articles of Association provide that appropriation of accrued profit is subject to the decision of the shareholders at the general meeting of shareholders. The Company can only make distributions to the shareholders and other persons entitled up to an amount, which does not exceed the amount of the distributable reserves. The general meeting may resolve to pay dividends from legally distributable reserves.

Independent auditor's report

To: the shareholder and Supervisory Board of Volkswagen Financial Services N.V.

A. Report on the audit of the financial statements 2017

Our opinion

We have audited the financial statements 2017 of Volkswagen Financial Services N.V., based in Amsterdam ('FSNV' or the 'Company').

WE HAVE AUDITED	OUR OPINION
The financial statements which comprise: 1. the balance sheet as at 31 December 2017; 2. the income statement for 2017; and 3. the notes comprising a summary of the applicable accounting policies and other explanatory information.	In our opinion the enclosed financial statements give a true and fair view of the financial position of Volkswagen Financial Services N.V. as at 31 December 2017 and of its result for 2017 in accordance with Part 9 of Book 2 of the Dutch Civil Code.

Basis for our opinion

We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. Our responsibilities under those standards are further described in the 'Our responsibilities for the audit of the financial statements' section of our report.

We are independent of Volkswagen Financial Services N.V. in accordance with the EU Regulation on specific requirements regarding statutory audit of public-interest entities, the "Wet toezicht accountantsorganisaties" (Wta), the "Verordening inzake de onafhankelijkheid van accountants bij assurance-opdrachten" (ViO) and other relevant independence regulations in the Netherlands. Furthermore, we have complied with the "Verordening gedrags- en beroepsregels accountants" (VGBA).

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Materiality

Based on our professional judgment we determined the materiality for the financial statements as a whole at € 65 million. The materiality has been calculated as 1% of the total assets which is the primary consideration of the users of the financial statements of the Company. We have also taken into account misstatements and/or possible misstatements that in our opinion are material for qualitative reasons for the users of the financial statements.

We agreed with the Supervisory Board that misstatements in excess of € 3.25 million, which are identified during the audit, would be reported to them, as well as smaller misstatements that in our view must be reported on qualitative grounds.

Our key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements. We have communicated the key audit matters to the Supervisory Board. The key audit matters are not a comprehensive reflection of all matters discussed.

These matters were addressed in the context of our audit of the financial statements as a whole and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

VALUATION OF LOANS	OUR AUDIT APPROACH
<p>As discussed in Note 1.1 to the financial statements, the main purpose of FSNV is the financing of companies and joint ventures belonging to the Volkswagen Financial Services AG group ('Volkswagen Group') through offering bonds and issuing commercial papers. The repayment of these financial liabilities is being guaranteed by Volkswagen Financial Services AG.</p> <p>We considered the valuation of the financial instruments granted to related parties as a key audit matter due to the size of the portfolio which consists of loans to (€ 3.2 billion) and receivables due from (€ 3.2 billion) Volkswagen Group companies and joint ventures as of year-end and due to the material impact an impairment may have on the income statement. These are initially recognized at fair value and subsequently measured at amortized cost. The estimation process is considered complex and significant judgements are made by management in ascertaining the provision for impairment. In particular, judgement arises over the determination of objective evidence of impairment which may have a reliably measurable effect on the present value of estimated future cash flows.</p> <p>In 2015, there were irregularities identified by US authorities relating to nitrogen oxide emissions on certain Volkswagen diesel engines. This prompted Standard & Poor's</p>	<p>The following procedures were performed to identify potential impairment triggers that affects the valuation of loans:</p> <ol style="list-style-type: none"> 1. Discussed the impairment analysis with management and Supervisory Board and challenged the assumptions used by comparing them with external observable data (e.g., data from credit rating agencies and financial data of the debtors); 2. Analyzed if there have been any impairment triggers at an individual loan level by challenging the fair values determined by management; 3. Tested the acceptability of impairment analysis method used by management by validating the mathematical accuracy and consistency of the method per counterparty. <p>Further, we have also reviewed the latest financial information of Volkswagen Financial Services AG and discuss with its external auditors to assess its ability to cover the repayment of financial securities issued by FSNV in case of default. We assessed the adequacy of the disclosures in the financial statements relating to these financial instruments.</p>

<p>and Moody's Investor Services to downgrade the credit rating of Volkswagen Financial Services AG. This has an impact to the creditworthiness of the entities within Volkswagen Group with existing loan balances due to FSNV and therefore could affect the valuation of the related accounts.</p> <p>Based on the impairment assessment performed by FSNV, management has concluded that no impairment is necessary as of year-end.</p>	
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APPROPRIATENESS OF HEDGE ACCOUNTING	OUR AUDIT APPROACH
<p>FSNV entered into derivative contracts to manage its interest rate risks and currency risks relating to the financial instruments issued by the Company as well as the loans granted to Volkswagen Group companies.</p> <p>FSNV's portfolio consists of forward contracts, long-term interest rate swaps and cross currency swaps. As of year-end, the notional amounts of the derivative instruments totaled EUR 5.8 billion.</p> <p>As discussed in Note 2.11, FSNV applies cost price hedge accounting to its derivative transactions. Management assessed that the hedge is 100% effective by comparing the critical qualitative characteristics of the hedged item and the hedging instrument (derivatives).</p> <p>We have identified this as a key audit matter since inappropriate application of the hedging will have an impact to the income statement.</p>	<p>Our audit procedures included evaluating and validating the design and operating effectiveness of controls over treasury transactions, including key reconciliation and management review of the derivative transactions with authorized banks.</p> <p>The following procedures were performed to ascertain that the use of hedge accounting is appropriate:</p> <ol style="list-style-type: none"> 1. Discussed with management the rationale for their expectation at the inception of the hedge that the hedging relationship will be highly effective and their process for reviewing its ongoing effectiveness. 2. Reviewed the documentation and hedge effectiveness testing performed by the management to ensure that the hedged transactions comply with the hedge accounting requirements, including designation and documentation requirements.

B. Report on other information included in the annual report

Next to the financial statements and our opinion thereon, the annual report consists of other information, including:

- ▶ the Supervisory Board report;
- ▶ the management report; and
- ▶ the other information on page 37.

Based on the procedures as mentioned below, we are of the opinion that the other information:

- ▶ is consistent with the financial statements and contains no material deficiencies;
- ▶ includes all information as required by Part 9 of Book 2 of the Dutch Civil Code.

We have read the other information and based on our knowledge and understanding obtained from the audit of the financial statements or otherwise, we have considered if the other information contains material deficiencies.

With these procedures, we have complied with the requirements of Part 9 of Book 2 of the Dutch Civil Code and the Dutch Auditing Standard 720. These procedures do not have the same scope as our audit procedures on the financial statements.

Management is responsible for the preparation of the other information including the preparation of the management report and the other information on page 37 in accordance with Part 9 of Book 2 of the Dutch Civil Code.

C. Report on other legal and regulatory requirements

Engagement

We were engaged by the Supervisory Board as auditor of Volkswagen Financial Services N.V. on 29 September 2016 as of the audit for year 2016 and have operated as statutory auditor ever since that financial year.

No prohibited non-audit services

We have not provided prohibited non-audit services as referred to in Article 5 (1) of the EU Regulation on specific requirements regarding statutory audit of public-interest entities.

D. Description of responsibilities for the financial statements

Responsibilities of management and the Supervisory Board for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with Part 9 of Book 2 of the Dutch Civil Code. Furthermore, management is responsible for such internal control as management determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to errors or fraud.

As part of the preparation of the financial statements, management is responsible for assessing the Company's ability to continue as a going concern. Based on the financial reporting framework mentioned, management should prepare the financial statements using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so. Management should disclose events and circumstances that may cast significant doubt on the Company's ability to continue as a going concern in the financial statements.

The Supervisory Board is responsible for overseeing the Company's financial reporting process.

Our responsibilities for the audit of the financial statements

Our objective is to plan and perform the audit assignment in a manner that allows us to obtain sufficient and appropriate audit evidence for our opinion.

Our audit has been performed with a high, but not absolute, level of assurance, which means we may not have detected all material errors and fraud.

Misstatements can arise from errors or fraud and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements. The materiality affects the nature, timing and extent of our audit procedures and the evaluation of the effect of identified misstatements on our opinion.

We have exercised professional judgment and have maintained professional skepticism throughout the audit, in accordance with Dutch Standards on Auditing, ethical requirements and independence requirements. Our audit included e.g.:

- ▶ Identifying and assessing the risks of material misstatement of the financial statements, whether due to errors or fraud, designing and performing audit procedures responsive to those risks, and obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from errors, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- ▶ Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- ▶ Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Concluding on the appropriateness of management's use of the going concern basis of accounting, and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company ceasing to continue as a going concern.
- ▶ Evaluating the overall presentation, structure and content of the financial statements, including the disclosures.
- ▶ Evaluating whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Supervisory Board regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant findings in internal control that we identify during our audit. In this respect we also submit an additional report to the audit committee in accordance with Article 11 of the EU Regulation on specific requirements regarding statutory audit of public-interest entities. The information included in this additional report is consistent with our audit opinion in this auditor's report.

We provide the Supervisory Board with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Supervisory Board, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, not mentioning it is in the public interest.

Amstelveen, 6 March 2018

For and on behalf of BDO Audit & Assurance B.V.,

sgd.
drs. M.F. Meijer RA
