

# Report of the Supervisory Board

## COOPERATION OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD

During the 2018 financial year, the Supervisory Board comprehensively performed the duties assigned to it by law, the Articles of Association, Rules of Procedure and – with one exception – the recommendations of the German Corporate Governance Code (hereinafter referred to as the “Code”). We regularly advised and continually oversaw the Management Board in its management of the Company and dealt extensively with the operational and strategic development of the Group. The Management Board fulfilled its duty to inform and furnish us with periodic written and verbal reports containing timely and detailed information on all business transactions and events of significant relevance to the Company. The Management Board prepared these reports in collaboration with the respective departments. In our Committee meetings and plenary sessions, we had the opportunity to discuss the Management Board’s reports and the proposed resolutions in full. The Management Board answered our questions on strategic topics affecting the Company with a great level of detail and submitted the relevant documents in a timely manner. Any deviations from the business plan were thoroughly explained to us and we were directly involved at an early stage in all decisions relevant to the Company.

An appropriate resolution was passed when the Supervisory Board’s approval for individual actions was required by law, the Articles of Association or the Rules of Procedure. The Supervisory Board members approved all actions by the Management Board requiring Supervisory Board approval based on the documentation provided in advance by the Management Board. When necessary, the Supervisory Board received the support of the relevant committees and, together with the Management Board, discussed any projects requiring decision. All matters requiring approval were submitted for review by the Management Board to the Supervisory Board on a timely basis.

Outside of the meetings of the Supervisory Board plenum and the Committees, the chairman of the Supervisory Board regularly exchanged information and ideas with the Management Board and especially the Chief Executive Officer, Dr. Simon Moroney. The Supervisory Board chairman was always kept promptly informed of the current business situation and any significant business transactions. The other Supervisory Board members also had regular contact with the individual Management Board members.

## SUPERVISORY BOARD MEETINGS IN THE 2018 FINANCIAL YEAR AND KEY ITEMS OF DISCUSSION

A total of eight Supervisory Board meetings were held in the 2018 financial year, whereby two meetings were conducted by telephone. With the exception of one meeting, all Supervisory Board members were present at all Supervisory Board meetings. In urgent cases occurring outside of meetings, the Supervisory Board passed resolutions by written procedure.

In addition to the above, a one-day strategy meeting took place between the Management Board and the Supervisory Board in July 2018 that primarily addressed

- the Company’s strategic focus; and
- the further development of the Company’s product portfolio and its impact on the net assets, financial position and results of operations.

During the 2018 financial year, the Supervisory Board paid particular attention to the following topics and passed resolutions on these topics after a thorough review and discussion:

- evaluation of the Company’s achievement of the 2017 financial year corporate targets, an interim review and minor adjustments to the corporate targets defined by the Supervisory Board at the end of 2017 for the 2018 financial year and defining the corporate targets for the 2019 financial year;
- commencing and executing an initial public offering in the United States of up to 8,300,000 American Depositary Shares (“ADSS”) pursuant to a Registration Statement on Form F-1 (“Initial Public Offering”) and granting the underwriters a 30-day option to purchase up to 1,245,000 additional ADSS following the offering (“Greenshoe”);
- increasing the share capital of the Company by issuing 2,075,000 new ordinary shares (each ADS representing 1/4 of a MorphoSys ordinary share, i.e. in total 8,300,000 ADSS) from the authorized capital 2017-II, excluding pre-emptive rights of existing shareholders, to implement the Initial Public Offering, and further increasing the share capital of the Company by issuing 311,250 additional new ordinary shares (each ADS representing 1/4 of a MorphoSys ordinary share, i.e. in total 1,245,000 ADSS) from the authorized capital 2017-II, excluding pre-emptive rights of existing shareholders, to implement the Greenshoe;

- modification of the rules of procedure of the Supervisory Board as well as the charter of the Audit Committee and the charter of Remuneration and Nomination Committee to reflect changes required by Nasdaq and US securities law;
- agenda and proposed resolutions for the 2018 Annual General Meeting, particularly the nominations of Dr. George Golumbeski, Michael Brosnan and Dr. Marc Cluzel as Supervisory Board candidates for election and re-election at the 2018 Annual General Meeting;
- election of the chair and re-election of the deputy chair of the Supervisory Board and establishment and staffing of the Committees in the Board's constituent meeting following the 2018 Annual General Meeting;
- award of the audit contract to the auditor for the 2018 financial year;
- founding of the subsidiary MorphoSys US Inc., which focuses on establishing the Company's commercial capabilities in the US;
- conclusion of a worldwide exclusive agreement between MorphoSys and Galapagos NV as licensors and Novartis Pharma AG as licensee covering the development and commercialization of our joint program MOR106;
- expansion of our strategic alliance to develop peptide-derived therapeutics with LEO Pharma;
- conclusion of a strategic partnering agreement with I-Mab granting exclusive rights to develop and commercialize our novel immuno-oncology agent MOR210 in China, Hong Kong, Macao, Taiwan and South Korea;
- budget for the 2019 financial year.

We also passed a resolution in the Supervisory Board plenum on the remuneration of Management Board members for the period July 1, 2018 to June 30, 2019 taking external benchmarking into consideration. We evaluated the achievement of the 2017 corporate targets that were agreed with the Management Board and discussed the corporate targets for 2019. We commissioned an independent remuneration consultant to confirm the appropriateness of the Management Board's compensation and its comparison to the remuneration of various levels of employees. We discussed and adopted the key performance indicators for the long-term incentive plans for both the Management Board and the Senior Management Group. Furthermore, we approved the financial statements for the 2017 financial year and dealt with the Corporate Governance Report and the Statement on Corporate Governance.

Our regular discussions in the Supervisory Board's plenary meetings were focused on MorphoSys's revenue and earnings development, the financial reports, the progress of the two business segments Partnered Discovery and Proprietary Devel-

opment, the results and progress of the clinical programs for the development of proprietary drugs, the future development strategy and the development of new technologies. Furthermore, we discussed the financial outlook for the 2020/2021 financial years and MorphoSys's associated future potential financing needs. In addition, we carried out an efficiency review of the Supervisory Board's work. And lastly, we kept ourselves regularly informed with respect to the Company's cash investment policy, risk management, internal audit results, internal control system and compliance management system.

#### **CONFLICTS OF INTEREST WITHIN THE SUPERVISORY BOARD**

No conflicts of interest arose within the Supervisory Board in the 2018 financial year.

#### **ACTIVITIES AND MEETINGS OF SUPERVISORY BOARD COMMITTEES**

To ensure that its duties are performed efficiently, the Supervisory Board has established three committees - the Audit Committee, the Remuneration and Nomination Committee and the Science and Technology Committee - to prepare the issues that fall within the Supervisory Board's respective areas of responsibility for the Supervisory Board plenum. In each Supervisory Board meeting, the chairs of the Committees report to the Supervisory Board on the Committees' work. The minutes of the Committee meetings are made available to all Supervisory Board members. The composition of these committees can be found in the "Statement on Corporate Governance," which is available on the Company's website under the heading "Media & Investors > Corporate Governance > Statement on Corporate Governance," and in the Annual Report on pages 85 to 90.

The Audit Committee met on five occasions in the 2018 financial year, one of those meetings was held by telephone. All Committee members were present at all Audit Committee meetings. The Committee dealt mainly with accounting issues, quarterly reports, financial statements and consolidated financial statements. The Committee discussed these topics with the Management Board and recommended the approval of the financial statements to the Supervisory Board. The auditor took part in four Audit Committee meetings and informed its members of the audit results. Against the background of the Auditors Reform Act and the requirements for the external and internal rotation of the auditor, in 2017 the Audit Committee carried out a public tender for the 2018 annual audit on a voluntary basis. As a result, the Audit Committee made a recommendation to the Supervisory Board with respect to the Supervisory Board's proposal at the Annual General Meeting for the election of the independent auditor for the 2018 financial year. In addition, the

Audit Committee dealt with the annual update of a list of permitted and pre-approved non-audit services of the auditor. The Committee also discussed the risk management system, the compliance management system and the results of the internal audit conducted in the 2018 financial year, as well as specific accounting issues under International Accounting Standards (IFRS) relevant to the Company. In addition, the Committee regularly discussed the Company's asset management policy and the investment recommendations made by the Management Board. The Committee also discussed in depth the 2019 budget and the financial outlook for the 2020/2021 financial years, as well as options for the commercialization strategy for the Company's most advanced proprietary drug candidate MOR208. In addition, the Audit Committee discussed in depth IT security measures undertaken in 2018 and the company's plan to change the ERP landscape from Microsoft Dynamics AX to SAP Business by Design. As in previous years, the Audit Committee discussed the proposed impairment tests in preparation for the annual audit.

To increase efficiency, there is a joint Remuneration and Nomination Committee, which deliberates on matters relating to remuneration and nomination. The Committee met on five occasions in the 2018 financial year, each time by telephone. All Committee members participated at all Committee meetings. In its function as a remuneration committee, the Committee mainly dealt with the Management Board's remuneration system and level of compensation. In this context, the Committee also commissioned an independent remuneration expert with the task of preparing a Management Board remuneration report to verify the appropriateness of the Management Board's remuneration. Based on this report, the Committee prepared a recommendation on the future structure of the Management Board's compensation and submitted this to the Supervisory Board for approval. The Committee also dealt with the ratio of compensation between the Management Board and the Senior Management Group and the staff overall and had this ratio reviewed by the commissioned remuneration expert. This expert confirmed the appropriateness of these "vertical" compensation ratios. In addition, the Committee gave careful consideration to the corporate targets as a basis for the Management Board's short-term variable remuneration and offered appropriate recommendations to the Supervisory Board for resolution. The Committee discussed the key performance indicators of the long-term incentive plans for the Management Board, Senior Management Group and other employees in key positions. In its function as the Nomination Committee, the Committee recom-

mended the re-appointment of Dr. Malte Peters as Chief Development Officer for the duration of three years, effective July 1, 2019 until June 30, 2022. In addition, this Committee dealt with succession planning within the company.

The Science and Technology Committee met on five occasions during the 2018 financial year. All Committee members participated in all Committee meetings. The Committee dealt mainly with the Company's discovery activities as well as overall strategy to expand the proprietary drug pipeline, the development of new technologies, the Company's drug development plans and future development strategy, progress in the clinical trials as well as required budget resources. One major focus was the approval strategy for MOR208 and the interactions with the FDA. The Committee also addressed the production of clinical trial and commercial materials for the Company's proprietary drug candidates including readiness for commercial supply and the competitive and patent situations of the Company's proprietary drug candidates. Finally, the Committee discussed the development and partnering of MOR106 as well as the further development of MOR202 in autoimmune diseases.

#### CORPORATE GOVERNANCE

The Supervisory Board devoted its attention to the further development of MorphoSys's corporate governance, taking into consideration the Code's amendments made by the Regierungskommission Deutscher Corporate Governance Kodex (Government Commission for the German Corporate Governance Code) in February 2017. The detailed Corporate Governance Report, including the Corporate Governance Statement according to Section 289f HGB and the Group Statement on Corporate Governance according to Section 315d HGB (German Commercial Code), can be found on the Company's website under the heading "Media & Investors > Corporate Governance > Corporate Governance Report" and in the Annual Report on pages 84 to 112.

We also discussed with the Management Board the Company's compliance with the Code's recommendations and in one justified case approved an exception to the Code's recommendations. Based on this consultation, the Management Board and the Supervisory Board submitted the annual Declaration of Conformity on November 30, 2018. The current version of the Declaration of Conformity can be found in this Annual Report and is permanently available to MorphoSys's shareholders on the Company's website under the heading "Media & Investors > Corporate Governance > Declaration of Conformity."

#### **CHANGES IN THE COMPOSITION OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD**

There were no changes in the composition of the Management Board during the reporting period.

However, the Chief Executive Officer, Dr. Simon Moroney, informed the Supervisory Board on February 19, 2019 that he has decided not to renew his contract as a member of the company's Management Board. As a result of his decision, Dr. Moroney will step down as CEO on expiry of his current contract on June 30, 2020, or when a successor is appointed, whichever comes sooner.

The following changes in the composition of the Supervisory Board took place during the reporting period. Klaus Kühn resigned from his office as a member of the Supervisory Board for personal reasons as of the conclusion of the 2018 Annual General Meeting. Dr. Marc Cluzel was re-elected and Dr. George Columbeski and Michael Brosnan were newly elected to the Supervisory Board by the 2018 Annual General Meeting.

#### **AUDIT OF THE ANNUAL FINANCIAL STATEMENTS AND CONSOLIDATED FINANCIAL STATEMENTS**

For the 2018 financial year, the Company commissioned PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Munich ("PwC") as its auditor. The audit contract was awarded by the Supervisory Board in accordance with the resolution of the Annual General Meeting on May 17, 2018. In accordance with Item 7.2.1 of the Code, the Supervisory Board obtained a declaration of independence from the auditor in advance.

The annual financial statements and the consolidated financial statements of MorphoSys AG, as well as the Management Report and Group Management Report for the 2018 financial year, were properly audited by PwC and issued with an unqualified Auditor's Report. The key topics of the audit for the consolidated and annual financial statements for the 2018 financial year were the revenue accounting for complex out-licensing arrangements and the completeness of revenue recognition in general, the measurement of the carrying amounts of goodwill and intangible assets that have indefinite useful lives, the recognition and measurement of the 2018 share-based payment programs, the accounting for accruals for outstanding invoices for external laboratory funding and external services, the presentation and measurement of financial assets, the effectiveness of internal controls, as well as the capital increase in connection with the US Initial Public Offering on the Nasdaq (dual listing).

In addition, the auditor confirmed that the Management Board had established an appropriate reporting and monitoring system that is suitable in its design and administration for the early detection of developments that could threaten the Company's existence.

The audit reports and documents relating to the annual financial statements and consolidated financial statements were provided on a timely basis to all Supervisory Board members for review. The audit report, the consolidated financial statements, the Group Management Report of the MorphoSys Group and the audit report, the annual financial statements and the Management Report of MorphoSys AG were discussed in detail at the Audit Committee meeting on March 12, 2019, and the meeting of the Supervisory Board on March 13, 2019. The auditor attended all meetings concerning the financial statements and quarterly statements and reported on the key results of his audit. The auditor also explained the scope and focus of the audit and was available to the Audit Committee and the Supervisory Board to answer questions and provide further information.

The Audit Committee discussed the audit results in detail and recommended to the Supervisory Board that it approve the financial statements prepared by the Management Board. The Supervisory Board also took note of the audit results and, in turn, reviewed the financial statements and management reports in accordance with the statutory provisions. Following its own examination, the Supervisory Board also determined that it sees no cause for objection. The annual financial statements and consolidated financial statements prepared by the Management Board and reviewed by the auditor, as well as the Management Report and Group Management Report, were subsequently approved by the Supervisory Board. Thus, the annual financial statements were adopted.

#### **RECOGNITION FOR DEDICATED SERVICE**

On behalf of the entire Supervisory Board, I would like to thank the members of the Management Board and the employees of MorphoSys for their achievements, their dedicated service and the inspirational work environment witnessed during this past financial year. Through their efforts, MorphoSys's portfolio has continued to mature and expand and important milestones have been achieved.

Planegg, March 13, 2019



Dr. Marc Cluzel  
Chairman of the Supervisory Board