



LEGO System A/S

**Aastvej 1, 7190 Billund
CVR no: 47 45 87 14**

Annual report 2022

Approved at the Company's Annual
General Meeting on 25 April 2023.

**Chairman of the meeting:
Poul Hartvig Nielsen**

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Financial Highlights

Over a 5-year period, the development can be described by the following financial highlights:

	2022	2021	2020	2019	2018
	mDKK	mDKK	mDKK	mDKK	mDKK
Statement of Profit or Loss					
Revenue	48,295	40,925	31,499	28,197	27,355
Operating profit	16,316	14,921	10,519	9,391	9,786
Profit before financial items	14,722	13,458	9,484	8,577	9,132
Financial income and expenses	-403	196	-66	-151	91
Net profit	11,370	10,673	7,286	6,570	7,199
Statement of Financial Position					
Net assets	41,336	37,005	32,607	28,466	28,406
Equity	18,310	16,622	14,201	14,296	14,721
Purchase of tangible fixed assets	1,822	1,313	909	885	661
Average number of employees					
	4,958	4,409	4,018	3,808	3,593
Financial ratios (in %)					
Gross margin	55.2%	57.1%	55.2%	53.8%	53.6%
Net profit margin	30.5%	32.9%	30.1%	30.4%	33.4%
Return on invested capital (ROIC)	35.6%	36.4%	29.1%	30.1%	32.1%
Solvency ratio	44.3%	44.9%	43.6%	50.2%	51.8%
Return on equity (ROE)	65.1%	69.3%	51.1%	45.3%	50.0%

The Financial Highlights are affected by the implementation of IFRS 16 Leases as from 1 January 2019. Comparison figures for 2018 have not been restated due to the use of the modified retrospective approach.

Definitions of Financial Highlights are stated in the section for accounting policies.

Company details

The Company

LEGO System A/S
Aastvej 1
7190 Billund, Denmark

Telephone: +45 79 50 60 70
Homepage: www.LEGO.com

CVR no: 47 45 87 14
Incorporated: 1 July 1973
Financial year: 1 January - 31 December
Residence: Billund

Parent Company

LEGO A/S, Billund (CVR no: 54 56 25 19)

Board of Directors

Carsten Rasmussen, chairman
John Hansen
Poul Hartvig Nielsen
Nanna Birgitta Gudum
Berit Flindt Pedersen
Jesper Laursen

Executive Board

Jesper Andersen

Auditor

PricewaterhouseCoopers
Statsautoriseret Revisionspartnerselskab

Management's Review

Business activities

The Company's main activity is the development, production, marketing, and sale of play materials.

Financial review

2022 was a year with double-digit growth for the LEGO Group and LEGO System A/S. For LEGO System A/S revenue for the full year increased 18 percent to DKK 48,295 million. Net profit was DKK 11,370 million in 2022 against DKK 10,673 million in 2021.

Revenue grew double digits, and ahead of 2022 plans, which anticipated single digit growth. Revenue growth was driven by strong consumer demand for the LEGO Group's portfolio which appealed to builders of all ages, skills and interests. Net profit is in line with 2022 expectations, which anticipated single digit growth.

Net profit was impacted by inflation, currency fluctuations, supply constraints and cease of commercial operations in Russia due to the war in Ukraine, which negatively impacted the net profit.

Management considers the Company's financial performance in the year satisfactory.

Outlook

The Company expects single digit revenue growth in 2023, ahead of the global toy market. This is expected to be achieved through continued focus on innovating portfolio and retail and e-commerce platforms. Expectations for net profit in 2023 is a result on level with 2022, as uncertainties still are expected, as well as costs associated with strategic initiatives will increase, to ensure short and long-term sustainable growth.

Management's review

Special risks – operational and financial risks.

Group management is responsible for the ongoing risk management, including mapping and assessment of risks as well as risk-minimising measures.

Risk management operates in four areas: strategic, financial, operational and disaster risks.

The work with risks continues to follow the policies and strategies adopted by the board for the areas. For these areas, systematic identification, assessment and coverage/handling are carried out in accordance with the strategies. A comprehensive overview of all the company's significant risks has been established in a consolidated risk matrix, where the effect and probability of an episode are mapped and prioritised, just as the consolidated risk exposure is measured and reported.

LEGO System A/S's most significant risks relate to the significant uncertainties in the toy market with significant volatility around the launch of new product concepts.

The overall risk exposure is still assessed as moderate in relation to the adopted risk appetite.

Currency risks

Currency risks are managed centrally on the basis of the board's approved currency policy. Future contracts and options are used to hedge purchases and sales in foreign currencies. As a general rule, these are classified as hedges and meet the accounting requirements for securing future cash flows.

Interest rate risks

The interest rate risk relates to interest-bearing liabilities and receivables. The interest rate risk is considered to be insignificant and is not expected to affect the result significantly.

Credit risks

Credit risks relate to receivables from sales and services. The LEGO Group has fixed credit granting procedures. The company has no significant receivables from sales and services concentrated in specific countries. As a result, the total credit risk is assessed to be low.

Disaster risks

Disaster risks cover situations that can paralyse the company's operations. The LEGO Group has continuity plans that ensure production; there is also an extensive insurance program that supports in the event of disasters. The Group has a crisis management group that can come together so that a possible disaster can be handled in the best possible way.

Management's review

Basis for earnings

Research and development (R&D)

Continuous innovation and development are key to the company's aspiration to inspire the builders of tomorrow. In 2022, new products account for 48 percent of the portfolio. The LEGO Group invests in innovating core play themes, exploring new play patterns as well as understanding the intersection between digital and physical play and creating new products to meet these changing needs. R&D activities include developing new technologies to enable learning through play; trend spotting; anthropological studies; and collaborating with educational institutions to deepen the company's understanding of children's development.

Branches

The company has a smaller branch abroad, LEGO System A/S Latvijas filiāle "Baltic", domiciled in Riga, Latvia.

Statutory report on corporate social responsibility and underrepresented gender

The LEGO Group aims to have a positive impact on its stakeholders and its local communities. In 2003, the LEGO Group signed the United Nations Global Compact to demonstrate its support of human rights, labour standards, anti-corruption, and the environment. The LEGO Group's 2022 Sustainability Progress Report (COP report) describes how it is working to adhere to the Compact. Pursuant to sections 99a and 99b of the Danish Financial Statements Act, the 2022 Sustainability Progress Report constitutes the statutory statement of corporate social responsibility.

This also includes information about the required quantitative targets for the under-represented gender on the Board of Directors in the LEGO Group. The 2022 Sustainability Progress Report is available at: [LEGO.com/AboutUs/Sustainability/Reporting](https://www.lego.com/AboutUs/Sustainability/Reporting).

Management's review

Data ethics policy

The LEGO Group is committed to handle data responsibly. The company has worked with data ethics around four key principles which are that data must be used within the company in a positive, fair, clear, and responsible way. More on the LEGO Group's principles regarding data ethics can be found at: LEGO.com./AboutUs/Policies-and-reporting/Policies.

Intellectual capital resources

The average number of employees in 2022 was 4,958 compared to 4,409 in 2021. Employees participate in the LEGO Group's Performance Management Programme. The programme is designed to ensure all colleagues work towards achieving the LEGO Group's short and long-term ambitions. Employees have targets that are aligned to the Group's overall targets and are awarded a bonus based on performance versus target.

Statement by the Executive Board and Board of Directors

The Executive Board and Board of Directors have today considered and adopted the annual report of LEGO System A/S for the financial year 1 January to 31 December 2022.

The Financial Statements has been prepared in accordance with the Danish Financial Statements Act.

In our opinion, the Financial Statements give a true and fair view of the financial position at 31 December 2022 of LEGO System A/S and of the results of LEGO System A/S's operations for the financial year 1 January to 31 December 2022.

In our opinion, the Management's Review includes a true and fair view of the development in the operations and financial circumstances of LEGO System A/S, of the result for the year and of the financial position of LEGO System A/S.

We recommend that the annual report be adopted at the Annual General Meeting.

Billund, 25 April 2023

Executive Board

Jesper Andersen

Board of Directors

Carsten Rasmussen
chairman

John Hansen

Poul Hartvig Nielsen

Nanna Birgitta Gudum

Berit Flindt Pedersen
(staff representative)

Jesper Laursen
(staff representative)

Independent auditor's report

To the Shareholders of LEGO System A/S

Opinion

In our opinion, the Financial Statements give a true and fair view of the financial position of the Company at 31 December 2022, and of the results of the Company's operations for the financial year 1 January - 31 December 2022 in accordance with the Danish Financial Statements Act.

We have audited the Financial Statements of LEGO System A/S for the financial year 1 January - 31 December 2022, which comprise Statement of Profit or Loss, Statement of Financial Position, Statement of Changes in Equity and notes, including a summary of significant accounting policies ("Financial Statements").

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs) and the additional requirements applicable in Denmark. Our responsibilities under those standards and requirements are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (IESBA Code) and the additional ethical requirements applicable in Denmark, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Statement on Management's Review

Management is responsible for Management's Review.

Our opinion on the Financial Statements does not cover Management's Review, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the Financial Statements, our responsibility is to read Management's Review and, in doing so, consider whether Management's Review is materially inconsistent with the Financial Statements or our knowledge obtained during the audit, or otherwise appears to be materially misstated.

Moreover, it is our responsibility to consider whether Management's Review provides the information required under the Danish Financial Statements Act.

Based on the work we have performed, in our view, Management's Review is in accordance with the Financial Statements and has been prepared in accordance with the requirements of the Danish Financial Statements Act. We did not identify any material misstatement in Management's Review.

Management's Responsibilities for the Financial Statements

Management is responsible for the preparation of Financial Statements that give a true and fair view in accordance with the Danish Financial Statements Act, and for such internal control as Management determines is necessary to enable the preparation of Financial Statements that are free from material misstatement, whether due to fraud or error.

In preparing the Financial Statements, Management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting in preparing the Financial Statements unless Management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the Financial Statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs and the additional requirements applicable in Denmark will always detect a material misstatement when it exists. Misstatements can arise from fraud or error 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.

As part of an audit conducted in accordance with ISAs and the additional requirements applicable in Denmark, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the Financial Statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain 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 error as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain 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.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by Management.

- Conclude on the appropriateness of Management's use of the going concern basis of accounting in preparing the Financial Statements 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 to cease to continue as a going concern.
- Evaluate the overall presentation, structure and contents of the Financial Statements, including the disclosures, and whether the Financial Statements represent the underlying transactions and events in a manner that gives a true and fair view.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Aarhus, 25 April 2023

PricewaterhouseCoopers

Statsautoriseret Revisionspartnerselskab

CVR no: 33 77 12 31

Mads Melgaard
State Authorised Public Accountant
mne34354

Thomas Bernth Jensen
State Authorised Public Accountant
mne47814

Statement of Profit or Loss

1 January - 31 December

	Note	2022 mDKK	2021 mDKK
Revenue	1	48,295	40,925
Production costs		-21,641	-17,545
Gross profit		26,654	23,380
Sales and distribution expenses		-7,592	-5,802
Administrative and IT expenses		-2,746	-2,657
Operating profit		16,316	14,921
Other operating expenses		-1,594	-1,463
Profit before financial items		14,722	13,458
Financial income	2	587	272
Financial expenses	3	-990	-76
Profit before tax		14,319	13,654
Income tax expenses	4	-2,949	-2,981
Net profit		11,370	10,673

Statement of Financial Position

at 31 December

Assets

	Note	2022 mDKK	2021 mDKK
Development projects in progress		126	51
Patents and other rights		0	0
Development projects and software		17	30
Intangible assets	5	143	81
Land and buildings		589	563
Plant and machinery		2,283	2,061
Other fixtures and fittings, tools and equipment		293	209
Fixed assets under construction		1,246	645
Propert, plant and equipment	6	4,411	3,478
Rental of premises		1,859	1,858
Other assets		143	135
Right-of-use assets	7	2,002	1,993
Total non-current assets		6,556	5,552
Inventories	8	3,522	2,126
Trade receivables		399	288
Receivables from related parties		28,959	27,728
Other receivables		1,391	818
Deferred tax	10	0	66
Receivables		30,749	28,900
Cash at banks		509	427
Total current-assets		34,780	31,453
Total assets		41,336	37,005

Statement of Financial Position

at 31 December

Liabilities

	Note	2022 mDKK	2021 mDKK
Share capital	9	50	50
Reserve for development costs		112	63
Reserve for hedge accounting		157	-161
Retained earnings		8,991	6,670
Proposed dividend		9,000	10,000
Total equity		18,310	16,622
Deferred tax liabilities	10	26	0
Other provisions	11	74	46
Provisions		100	46
Borrowings	12	118	127
Lease liabilities	12	1,827	1,838
Payables to related parties	12	95	0
Total non-current liabilities		2,040	1,965
Borrowings	12	9	10
Lease liabilities	12	210	181
Trade payables		2,408	2,200
Payables to related parties	12	14,665	12,693
Income tax liabilities		232	18
Other debt		2,747	2,875
Deferred income	13	615	395
Total current liabilities		20,886	18,372
Total liabilities		22,926	20,337
Total equity and liabilities		41,336	37,005
Proposed distribution of profit	14		
Contingent liabilities and other obligations	15		
Employee costs	16		
Derivative financial instruments	17		
Related parties and ownership	18		
Events occurring after the reporting period	19		
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Statement of Changes in Equity

	Share capital	Reserve for develop- ment cost	Reserve for hedge accounting	Retained earnings	Proposed dividend	Total equity
	mDKK	mDKK	mDKK	mDKK	mDKK	mDKK
Equity at 1 January 2022	50	63	-161	6,670	10,000	16,622
Dividend paid	0	0	0	0	-10,000	-10,000
Adjustments development cost	0	49	0	-49	0	0
Fair value adjustments of derivative financial instruments	0	0	408	0	0	408
Tax on equity transactions	0	0	-90	0	0	-90
Profit for the year	0	0	0	2,370	9,000	11,370
Equity at 31 December 2022	50	112	157	8,991	9,000	18,310

Notes to the Financial Statements

	2022	2021
	mDKK	mDKK
1 Revenue		
Sale of goods	47,572	40,509
Licence income	723	416
	48,295	40,925
Sale of goods per region:		
Americas	21,355	16,629
Europe, Middle East & Africa	22,214	20,050
Asia & Pacific	4,003	3,830
	47,572	40,509
2 Financial income		
Interest income from related parties	577	267
Other interest income	10	5
	587	272
3 Financial expenses		
Interest expenses to related parties	107	24
Interest expenses related to lease liabilities	34	25
Exchange losses, net	811	24
Other interest expenses	38	3
	990	76

Notes to the Financial Statements

	<u>2022</u>	<u>2021</u>
	mDKK	mDKK
4 Income tax expenses		
Income tax charge for the year	3,166	3,060
Deferred tax change for the year	-1	-78
Adjustment to income tax for prior years	-219	0
Adjustment to deferred tax for prior years	3	-1
Total income tax expenses	<u>2,949</u>	<u>2,981</u>

Income tax expenses is impacted by adjustment to previous year's transfer pricing agreements with related parties within the LEGO Group.

The company is included in the joint taxation of the parent company, KIRKBI A/S.

5 Intangible assets

	Development projects in progress	Patents and other rights	Development projects and software
	mDKK	mDKK	mDKK
2022			
Cost at 1 January	51	324	529
Additions	75	0	15
Disposals	0	0	-12
Transfers	0	0	0
Cost at 31 December	<u>126</u>	<u>324</u>	<u>532</u>
Amortisation and impairment at 1 January	0	324	499
Amortisation for the year	0	0	28
Disposals	0	0	-12
Amortisation and impairment at 31 December	<u>0</u>	<u>324</u>	<u>515</u>
Carrying amount at 31 December	<u>126</u>	<u>0</u>	<u>17</u>
Useful lives:		<u>3-5 years</u>	<u>3-5 years</u>

Notes to the Financial Statements

5 Intangible assets (continued)

Development projects are included in the financial position with DKK 143 million. Development projects comprises expenses to developing products, with intention to be produced and sold under the LEGO brand, and internally developed software.

Patents and other rights comprises acquired productionrights on few LEGO brands. The brands, which relates to production rights, are still used in the company and the LEGO Group.

6 Property, plant and equipment

	Land and buildings	Plant and machinery	Other fixtures and fittings, tools and equipment	Fixed assets under construction
	mDKK	mDKK	mDKK	mDKK
2022				
Cost at 1 January	1,246	7,353	514	645
Additions	26	725	49	1,022
Disposals	-53	-329	-13	0
Transfers	43	294	84	-421
Cost at 31 December	<u>1,262</u>	<u>8,043</u>	<u>634</u>	<u>1,246</u>
Depreciation and impairment at 1 January	683	5,292	305	0
Depreciation for the year	42	788	46	0
Disposals	-52	-320	-10	0
Depreciation and impairment at 31 December	<u>673</u>	<u>5,760</u>	<u>341</u>	<u>0</u>
Carrying amount at 31 December	<u>589</u>	<u>2,283</u>	<u>293</u>	<u>1,246</u>
Useful lives:	<u>10 - 40 years</u>	<u>5 - 15 years</u>	<u>2 - 10 years</u>	

Notes to the Financial Statements

7 Right-of-use assets

	Rental of premises	Other assets
	mDKK	mDKK
2022		
Cost at 1 January	2,168	247
Additions and remeasurements	156	80
Disposals	-5	-55
Cost at 31 December	<u>2,319</u>	<u>272</u>
Depreciation and impairment at 1 January	310	112
Depreciation for the year	155	63
Disposals	-5	-46
Depreciation and impairment at 31 December	<u>460</u>	<u>129</u>
Carrying amount 31 December	<u>1,859</u>	<u>143</u>
Useful lives:	<u>10-25 years</u>	<u>2-8 years</u>
	2022	2021
	mDKK	mDKK

8 Inventories

Raw materials	871	397
Work in progress	1,340	836
Finished goods	1,311	893
	<u>3,522</u>	<u>2,126</u>

9 Share capital

The share capital comprise of:

20 shares of DKK 1,000	0	0
198 shares of DKK 10,000	2	2
290 shares of DKK 100,000	29	29
19 shares of DKK 1,000,000	19	19
	<u>50</u>	<u>50</u>

There has been no changes to the share capital for the past 5 years.

Notes to the Financial Statements

	<u>2022</u>	<u>2021</u>
	mDKK	mDKK
10 Deferred tax		
Deferred tax, net at 1 January	66	-83
Adjustment prior years	-3	1
Adjustment through equity	-90	70
Expensed change of the year	1	78
Deferred tax at 31 December	<u>-26</u>	<u>66</u>

Deferred tax is recognised in the Statement of Financial Position as follows:

Deferred tax assets	0	66
Deferred tax liabilities	26	0

Deferred tax reflects the effect of temporary difference between the carrying amount and the tax based amount primarily of non-current assets, inventories, accruals and the tax value of the forward exchange contracts. Deferred tax assets are recognised only to the extent that it is probable that future taxable profit will be available.

11 Other provisions

Other provisions comprise of various types of provisions, e.g. provisions for retirement obligations regarding leased premises and one offs.

Notes to the Financial Statements

12 Non-current liabilities

Repayments due within 1 year are listed under current liabilities. Remaining liabilities are recognised as non-current liabilities. The liabilities are due in accordance with the following order:

	2022	2021
	mDKK	mDKK
Borrowings		
After more than 5 years	81	86
Between 1 and 5 years	37	41
Non-current liabilities	118	127
Within 1 year	9	10
	127	137
Lease liabilities		
After more than 5 years	1,319	1,330
Between 1 and 5 years	508	508
Non-current liabilities	1,827	1,838
Within 1 year	210	181
	2,037	2,019

The company does not have significant sub-leasing contracts.

The company has not entered into any significant leases, not yet commenced, to which the company is committed (DKK 0 million in 2021).

	2022	2021
	mDKK	mDKK
Payables to related parties		
After more than 5 years	0	0
Between 1 and 5 years	95	0
Non-current liabilities	95	0
Within 1 year	0	0
Other current payables to related parties	14,665	12,693
Current liabilities	14,665	12,693
	14,760	12,693

Notes to the Financial Statements

13 Deferred income

Deferred income primarily comprise of obligations relating to VIP loyalty program.

	2022	2021
	mDKK	mDKK
14 Proposed distribution of profit		
Proposed dividend	9,000	10,000
Retained earnings	2,370	673
	11,370	10,673

15 Contingent liabilities and other obligations

Security has been given for land and buildings with a net carrying amount of DKK 503 million (DKK 474 million in 2021) for the company's mortgage loans totalling DKK 127 million (DKK 137 million in 2021).

	2022	2021
	mDKK	mDKK
Contractual obligations		
Bank guarantees	112	112
Purchase contract commitments of property, plant and equip.	1,936	822
Other obligations	2,008	3,601
	4,056	4,535

Other obligations consist of licence and service agreements.

The entity has entered various contracts with vendors on usual terms and conditions of sales.

The entity takes part in some legal cases. The management believe the outcome has no influence on the financial position.

The Danish companies in the LEGO Group are jointly and severally liable for corporate income tax according to the joint taxation in the LEGO Group, KIRKBI A/S and in the companies controlled by KIRKBI A/S. The total amount of income tax liabilities, as well as related income tax credit counterparts are shown in the Annual Report of KIRKBI A/S, which is the administration company of the joint taxation. The Danish companies in the LEGO Group are furthermore jointly and severally liable for Danish Taxes at source withheld on behalf of non-resident companies for dividend, royalty and interest.

Notes to the Financial Statements

	2022	2021
	mDKK	mDKK
16 Employee costs		
Salaries	3,886	3,727
Pension costs	269	216
Social security and other costs	91	76
	4,246	4,019

Remuneration to Board of Directors amounts to DKK 140,000 (DKK 140,000 in 2021). No separate remuneration is paid to Executive Board, who is paid in parent company LEGO A/S.

	2022	2021
Average number of full-time employees	4,958	4,409

17 Derivative financial instruments

Forward contracts and options are used to hedge purchases and sales in foreign currencies on future cash flow, comprises the following currencies in net amount (net of purchase/sale):

Currency	2022		2021	
	mDKK Contract amount	mDKK Fair value, net	mDKK Contract amount	mDKK Fair value, net
DKK/USD	7,165	24	5,954	-194
DKK/GBP	1,095	30	1,164	-21
DKK/AUD	1,085	21	1,138	-13
DKK/JPY	348	8	402	1
DKK/CAD	1,321	45	1,116	-26
DKK/CNY	592	15	935	-65
DKK/other	793	24	893	-6
	12,399	167	11,602	-324

Notes to the Financial Statements

17 Financial instruments continued

Fair value of derivative financial instruments constitutes at the end of the year

	2022	2021
	mDKK	mDKK
Assets	287	18
Liabilities	120	342

Forward exchange contracts cover a period of 0-12 months (0-12 months in 2021).

18 Related parties and ownership

Controlling interest

LEGO System A/S is through LEGO A/S owned by KIRKBI A/S (75%) and Koldingvej 2, Billund A/S (25%).

Transactions

All related party transactions are conducted on arm's length basis.

Consolidated Financial Statements

The entity is a part of the Consolidated Annual Report, made by LEGO A/S, Billund (CVR-no. 54 56 25 19), and in the Consolidated Annual Report made by KIRKBI A/S, Billund (CVR-no. 18 59 12 35), which is the ultimate parent.

19 Events occurring after the reporting period

No events of importance have occurred after the reporting date.

Notes to the Financial Statements

20 Accounting policies

Basis of preparation

The Financial Statements of LEGO System A/S have been prepared in accordance with the provisions of the Danish Financial Statements Act applying to enterprises of reporting class C (large).

In pursuance of §86(4) of the Danish Financial Statement Act, the company has not prepared a Statement of Cash Flow. Reference is made to the Consolidated Financial Statement of LEGO A/S.

Referring to §96(3) of the Danish Financial Statement Act, the company does not disclose the fee paid to the auditors appointed by the Annual General Meeting. The fee is included in the Consolidated Financial Statement of LEGO A/S.

The accounting policies for the Financial Statements remain unchanged from last year.

The Financial Statements are presented in million Danish kroner (mDKK).

Change in classification in the Statement of Profit or Loss

Comparative figures in the Statement of Profit or Loss have been restated to match this year's presentation. The adjustment of comparative figures has no effect on profit before tax.

Change in classification in the Statement of Financial Position

Comparative figures in the Statement of Financial Position have been restated to match this year's presentation. The adjustment of comparative figures has no effect on total assets.

The adjustments of comparative figures are not a change in accounting policies.

Foreign currency translation

Foreign currency transactions are translated into the presentation currency using the exchange rates prevailing at the date of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at balance sheet date exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Statement of Profit or Loss, except for derivative financial instruments, refer to section derivative financial instruments.

Other currencies than Danish kroner are considered foreign currencies.

Derivative financial instruments

LEGO System A/S uses a number of forward contracts and options to hedge currency exposure. The hedging activities are categorised into hedging of forecast transactions (cash flow hedges) and hedging of assets and liabilities (fair value hedges).

Notes to the Financial Statements

Derivative financial instruments are initially recognised at cost and are subsequently remeasured at their fair value at the balance sheet date. Positive and negative fair value of derivative financial instruments are recognised in financial income/expense in Statement of Profit or Loss.

The changes in the fair value of derivative financial instruments that are designated and qualify as cash flow hedges are recognised within a separate reserve under equity, other receivables and other debt. The cumulative gains or losses relating to these hedge transactions are reclassified from equity when the hedged item affects the Statement of Profit or Loss, or if the hedged transaction is no longer to take place.

For derivative financial instruments that do not meet the criteria to be classified as hedging instruments, the changes in fair value are recognised immediately in the Statement of Profit or Loss. When option contracts are used to hedge forecast transactions, the LEGO Group designates only the intrinsic value of the option contract as the hedging instrument.

Statement of Profit or Loss

Revenue

For revenue recognition, IFRS 15 is used as interpretation.

Revenue is recognised when the company fulfils its contractual performance obligations towards the buyer, and the transaction is related to the main activities.

Revenue from sale of goods

Revenue from sale of goods is recognised when control over the goods has been transferred to the buyer. This condition is usually met by the time the products are delivered to the customer and legal title transfers. Revenue is measured at the transaction price to which the LEGO Group expects to be entitled. Transaction price includes variable amounts (rebates, sales incentives and provisions for returned products etc.), thus the variable amount is recognised as revenue only when it is highly probable that a significant reversal will not occur. Provisions and accruals for rebates, sales incentives and return of products are made in the period in which the related sales are recorded. Historical data are readily available and reliable and are used for estimating the amount of the reduction in sales.

Sale of goods that results in award credits under the LEGO Group's consumer loyalty programme is accounted for by allocating the transaction price between the goods supplied and the award credits granted based on a relative stand-alone selling price. The loyalty programme is a separate performance obligation, as the loyalty programme points are considered a material right derived from the contract entered at the time of purchase. Revenue from the award credits is recognised when the points are redeemed or when they expire.

Revenue from royalty and licence agreements

Licence fees are recognised as revenue when the performance obligations in the relevant agreements have been satisfied. Revenue is measured at the transaction price to which the LEGO Group

Notes to the Financial Statements

expects to be entitled. Revenue from licence agreements comprises both agreements where performance obligations are satisfied over time such as sales-based agreements which most of the LEGO Group's licence revenue is related to, and agreements where performance obligations are satisfied at a point in time, which would normally be upon delivery. Licence revenue is recognised based on a classification of either a "right to access" or "right to use" as described below.

Right to access

Revenue derived from the LEGO® trademark is generally considered a "right to access" and performance obligations related to licence income of this nature are satisfied over time. Licences with a "right to access" comprise income from console games, movies, mobile and tablet platforms, and outbound licensing business generating sales-based royalty fees for intellectual properties related to content like stories, style guides and prints. Revenue based on a "right to access" is recognised based on the licensee's actual sales or forecasts, which in all material aspects corresponds with the value-add to the licence partner. The process is therefore assessed to give a faithful depiction of the transfer of licence income.

Right to use

All other licence revenues are per definition performance obligations satisfied at a point in time ("right to use"). Revenue is recognised at a point in time, where the customer directly uses and obtains substantially all the benefits from the licence, at the point when control is transferred to the licensee. Revenue recognised at a point in time will primarily be related to media content produced by the LEGO Group. Media content has significant standalone functionality and the LEGO Group does not affect the intellectual properties after the right to use occurs. Revenue is recognised when the control of the content has been transferred to the customer.

Production costs

Production costs include direct and indirect costs related to production including movements in volumes on inventory and related inventory re-evaluation. Direct costs comprise raw materials, consumables, trademark royalty and direct labour costs. Indirect costs comprise other costs related to production of goods including depreciation, amortisation and impairment on production related material and other supply chain related costs.

Sales and distribution expenses

Sales and distribution expenses comprise expenses related to sales and distribution staff, advertising and marketing expenses, write-down of receivables as well as depreciation, amortisation and impairment.

Administrative and IT expenses

Administrative and IT expenses comprise expenses for IT, Facility, Human Resources, Finance, Legal and Management, including depreciation, amortisation and impairment.

Notes to the Financial Statements

Other operating expenses

Other operating expenses comprise secondary expenses in relation to the company's primary activity, including gain and loss on sold tangible assets and research and development expenses that do not meet the criteria for asset recognition.

Research and development expenses

Research and development expenses are expensed in the Statement of Profit or Loss as they incur. Development projects that are clearly defined and identifiable and that are expected to generate future economic profit are recognised as intangible assets at cost less accumulated amortisation and write-downs. Development projects are amortised on a straight-line basis over the expected useful life, which is estimated at 3-5 years.

Financial income and expenses

Financial income and expenses are recognised with the amounts related to the period.

Financial items comprise interest income and expenses, realised and unrealised gains and losses on payables/receivables and transactions in foreign currencies, and fair value adjustments of derivative financial instruments.

Tax for the year

The tax expenses for the year comprise income tax and deferred tax for the year.

The income and deferred taxes are recognised in the Statement of Profit or Loss, except to the extent that they relate to items recognised in Statement of Changes in Equity. In this case, the tax is recognised in equity.

All Danish entities in the LEGO Group are taxed jointly. The current Danish corporation tax is distributed among the jointly taxed companies in relation to their taxable income (full distribution with refunds regarding tax-related deficits). Any changes in deferred tax due to changes in tax rates are recognised in the Statement of Profit or Loss.

Notes to the Financial Statements

Financial Position

Intangible assets

Development projects in progress are currently running projects, primarily within software development. Development projects in progress cover non-finalised projects at the balance sheet date. Development projects in progress that are clearly defined and identifiable, where the technical feasibility, sufficient resources and a potential future market or utilisation opportunity within the company is demonstrated, and where the company intends to produce, market or use the project, are recognised as intangible assets provided that the cost can be measured reliably and that there is sufficient assurance that future earnings or the net selling price can cover cost of sales, selling and distribution costs, administrative expenses and development costs. Other development costs are recognised in the Statement of Profit or Loss as incurred.

Recognised development costs are measured at cost less impairment. Cost includes direct and indirect expenses directly attributable to the asset until the asset is ready for use as intended.

Software comprises mainly internally developed software for the purpose of supporting business operations. Software is capitalised based on the costs incurred. Software and development projects are amortised on a straight-line basis over the expected useful life, which is estimated at 3-5 years. Residual value is set at DKK 0.

Software and development projects are tested for impairment in case of indications hereof and written down to the lower of recoverable amount and carrying amount.

Patents and other rights are capitalised based on the costs incurred. Patents and other rights are amortised over the shorter of their estimated useful lives and the contractual duration, which is usually 3-5 years. Residual value is set at DKK 0.

Property, plant and equipment

Land and buildings comprise mainly factories, warehouses and offices. Plant and machinery are mainly moulds, moulding machines, processing and packing equipment. Whilst other fixtures, fittings, tools and equipment mainly comprise high bay warehouse equipment, lease hold improvements, measuring and testing equipment, furniture and IT hardware.

Property, plant and equipment are measured at cost, less subsequent depreciation and impairment, except for land, which is measured at cost less impairment.

Cost comprises acquisition price and expenses directly related to the acquisition until the time when the asset is ready for use as intended. The cost of self-constructed assets comprises direct expenses such as wage consumption, materials and indirect expenses to the extent, that it directly supports the asset construction.

Notes to the Financial Statements

Subsequent expenditure for improvements and maintenance is allocated to the asset cost price if future economic benefits are likely. General repair and maintenance is expensed in the Statement of Profit or Loss as incurred.

Depreciation is calculated on a straight-line basis to allocate the cost of each asset to its residual value. Property, plant and equipment is tested for impairment when impairment indicators exist. Management performs an annual assessment of the assets' future use eg. in relation to changes in building, product and production setup or restructuring.

Depreciation is calculated based on the following estimated useful lives:

Buildings	10-40 years
High bay warehouses	40 years
Plant and machinery	5-15 years
Furniture, fittings and equipment	2-10 years

Land is not depreciated.

Depreciation commences when the asset is acquired or when the asset is ready for use as intended. Property, plant and equipment with cost below DKK 100,000 are expensed in the acquisition year.

Leases

For lease recognition, IFRS 16 is used as interpretation.

The right-of-use asset and corresponding lease liability are recognised at the commencement date, i.e. the date the underlying asset is available for use. The lease terms may include options to extend or terminate the lease when it is reasonably certain that the option will be exercised.

The LEGO Group applies the short-term lease recognition exemption for lease contracts that, at the commencement date, have a lease term of 12 months or less for all classes of underlying assets, and the exemption for lease contracts for which the underlying asset is of low value. Lease payments on short-term leases and leases of low-value assets are recognised as expense on a straight-line basis over the lease term.

The lease liabilities are initially measured at the present value of lease payments to be made over the lease term. The lease payments are discounted using the incremental borrowing rate. The lease payments include fixed payments and variable lease payments that depend on an index or a rate, less any lease incentives receivable. The lease liability is subsequently measured by increasing the carrying amount to reflect interest on the lease liability and by reducing the carrying amount to reflect the lease payments made. If the contract holds an option to purchase, extend or terminate a lease and it is reasonably certain to be exercised, the lease payments will include those.

Notes to the Financial Statements

The lease liability is remeasured (and makes a corresponding adjustment to the related right-of-use asset) whenever:

- The lease term has changed or there is a significant event or change in circumstances resulting in a change in the assessment of exercising an option, in which case the lease liability is remeasured by discounting the revised lease payments using a revised discount rate.
- The lease payments change due to changes in index or rate.
- A lease contract is modified and the lease modification is not accounted for as a separate lease, in which case the lease liability is remeasured based on the lease term of the modified lease by discounting the revised lease payments using a revised discount rate at the effective date of the modification.

Right-of-use assets are measured at cost corresponding to the lease liability recognised, adjusted for any lease incentives received and initial direct costs. Depreciation is calculated using the straight-line method over the lease term or the useful life of the right-of-use assets, whichever is shortest. The variable lease payments that do not depend on index or a rate are recognised as expense in the year the event or condition that triggers the payment occurs. For all classes of assets, non-lease components will be separated from the lease components and thereby not form part of the right-of-use asset and financial lease liability recognised in the Financial Position.

Inventories

Inventories are measured at the lower of cost and net realisable value. Cost is accounted for on a first-in, first-out basis (FIFO). Cost comprises direct materials, direct labour and an appropriate proportion of variable and fixed overhead expenditure (indirect production costs), the latter being allocated on the basis of normal production capacity. Costs of purchased inventory are determined after deducting rebates and discounts. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Receivables

Receivables are initially recognised at fair value equal to the transaction price, and subsequently measured at amortised cost less allowance for lifetime expected credit losses. Receivables are written off when all possible options have been exhausted and there are no reasonable expectations of recovery.

The company applies the IFRS 9 simplified approach to measure expected credit loss and a lifetime expected loss allowance for all trade receivables. Exposure to credit risk on trade receivables is guided by the LEGO Group's policy on managing credit risk. Credit limits are set based on the customer's financial position and current market conditions.

Cash at banks

Cash at banks comprise cash and cash-equivalents. Cash balances within the Group cash pool agreement are considered receivables and payables from/to related parties.

Notes to the Financial Statements

Equity

Proposed dividend

Dividend proposed for the year is recognised as a liability once adopted at the annual general meeting (declaration date). Dividends expected to be distributed for the financial year are presented as a separate item.

Reserve for development costs

The reserve for development costs comprises recognised development costs. The reserve cannot be used to distribute dividend or cover losses. The reserve will be reduced or dissolved if the recognised development costs are amortised or are no longer part of the company's operations by a transfer directly to the distributable reserves under equity.

Reserve for hedge accounting

The reserve for hedge accounting consists of the effective portion of gains and losses on hedging instruments designated as cash flow hedges.

Provisions

Provisions are recognised when the company identifies legal or constructive obligation as a result of past events, and it is probable that it will lead to an outflow of resources that can be reliably estimated. In this connection, the company makes the estimate based upon an evaluation of the individual most likely outcome of the cases. In cases where a reliable estimate cannot be made, these are disclosed as contingent liabilities.

Deferred tax

Deferred tax liabilities and deferred tax assets are measured according to balance sheet liabilities method, which means that all temporary differences between the carrying amount and the tax base of assets and liabilities are recognised in the Financial Position as deferred tax liabilities and deferred tax assets. Deferred tax reflects the effect of any temporary differences. To the extent calculated deferred tax is positive, this is recognised in the Statement of Financial Position as a deferred tax asset at the expected realisable value. Deferred tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred tax is measured according to income tax rules and the tax rates expected to be in force on elimination of temporary differences. The change in deferred tax as a result of changes in tax rates is recognised in the Statement of Profit or Loss. Changes to deferred tax on items in equity are recognised in equity.

Notes to the Financial Statements

Borrowings

Borrowings are initially recognised at fair value, net of transaction expenses incurred. Borrowings are subsequently measured at amortised cost. Any differences between the proceeds and the redemption value are recognised in the Statement of Profit or Loss over the period of the borrowings using the effective interest method.

Liabilities

Other liabilities are measured at amortised cost.

Deferred income

Deferred income recognised under liabilities comprise of income regarding subsequent financial reporting years, such as consumer loyalty programme and gift cards.

Financial ratios

The financial ratios stated under "Financial Highlights" have been calculated in accordance with the guidelines from the Danish Society of Financial Analysts:

Gross margin:
$$\frac{\text{Gross profit} \times 100}{\text{Revenue}}$$

Net profit margin:
$$\frac{\text{Profit before financial items} \times 100}{\text{Revenue}}$$

Return on invested capital:
$$\frac{\text{Profit before financial items} \times 100}{\text{Net assets}}$$

Solvency ratio:
$$\frac{\text{Equity} \times 100}{\text{Net assets}}$$

Return on equity (ROE):
$$\frac{\text{Net profit for the year} \times 100}{\text{Average equity}}$$