BANCA IFIS

# PUBLIC DISCLOSURE

# AT 31 DECEMBER 2018

# PILLAR 3

BANCA IFIS

**Banca IFIS S.p.A.**

Registered offices in Via Terraglio 63, 30174 Venice-Mestre, Italy

Venice Business Register and tax code no. 02505630109 – VAT no. 02992620274

REA (Administrative Economic Index) no. VE – 0247118

Share capital Euro 53,811,095 fully paid-up

Registered in the Banking Register with no. 5508

Parent Company of the Banca IFIS S.p.A. Banking Group, registered in the Register of Banking Groups

Member of the Italian Interbank Deposit Protection Fund

Website: *www.bancaifis.it*

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## INTRODUCTION

Effective 1 January 2014, the set of reform measures developed by the Basel Committee ("Basel 3") was transposed into the European Union legislation. These reforms aim at improving the banks' ability to absorb *shocks* arising from financial and economic stress, whatever the source, improving risk management and *governance*, and strengthening the banks' transparency and disclosure. The Basel Committee has maintained the three-pillar approach on which the previous agreement on capital ("Basel 2") was based. It integrated and strengthened it in order to increase, in qualitative and quantitative terms, the capital position of intermediaries by introducing countercyclical supervisory instruments, regulations on liquidity risk management and leverage limits.

In particular, the Third Pillar (hereinafter also "Pillar 3") is based on the assumption that the Market Discipline may contribute to strengthen capital regulations and therefore promote the stability and soundness of banks and the financial sector.

Therefore, the purpose of Pillar 3 is to combine the minimum capital requirements (Pillar 1) and the process of prudential monitoring (Pillar 2) through the identification of a set of disclosure transparency requirements which allow the market operators to be provided with relevant, comprehensive and reliable information about capital adequacy, exposure to risks and general characteristics of the systems intended to identify, measure and manage said risks.

Within the European Union, "Basel 3" measures have been transposed into two legislative acts:

- Directive 2013/36/EU of 26 June 2013 (hereinafter "CRD IV") endorsed by the Bank of Italy through Circular 285 of 17 December 2013 "Supervisory provisions for banks". These EU provisions govern, inter alia, the conditions for accessing banking activities, the freedom of establishment and the freedom to provide services, the supervisory review and additional capital buffers;
- EU Regulation no. 575/2013 of 26 June 2013 (hereinafter "CRR") which governs the prudential supervisory institutions set by Pillar 1 and the rules on public disclosure (Pillar 3).

The European Union legislation is supplemented by the provisions issued by the Bank of Italy, in particular with Circular no. 285 of 17 December 2013 (hereinafter "Circular No. 285/2013"), which contains the prudential supervisory provisions applicable to Italian banks and banking groups, revised and updated in order to adapt internal regulations to the changes in the international regulatory framework, with particular regard to the new regulatory and institutional framework for EU banking supervision, as well as to take into account the needs identified to ensure supervision of banks and other intermediaries.

The aforementioned Circular does not set out specific rules for the preparation and publication of *Pillar 3*, but merely reports the list of provisions for the purpose envisaged by the CRR. The matter, therefore, is directly regulated by:

- the CRR itself, Part 8 "Disclosure by institutions" (art. 431 - 455) and Part 10, Title I, Chapter 3 "Transitional provisions on disclosure of own funds" (art. 492);

- the Regulations of the European Commission, whose preparation is entrusted to the EBA (European Banking Authority), containing the Regulatory Technical Standard (RTS) and Implementing Technical Standard (ITS) to create standard models for the publication of different types of information.

Further indications were then provided by the EBA with a specific document concerning guidelines on materiality, proprietary and confidentiality and on the frequency of information to be provided in the Third Pillar (*EBA/GL/2014/14 - Guidelines on materiality, proprietary and confidentiality and on disclosures frequency under Articles 432 (1), 432 (2) and 433 of Regulation No (EU) 575/2013)* which regulates further relevant aspects in the preparation of the disclosure: (i) the implementation by the institutions of the criterion of materiality of the disclosure; (ii) the implementation by the institutions of the exclusivity and confidentiality of the disclosure; (iii) the need to publish information more than annually. Based on Art. 433 CRR, the information to the public which is required by Community legislation must be published by the banks at least once a year, together with the financial statements. The CRR does not explicitly require the publication of an interim report, leaving the banks the right to publish some or all of the information more frequently. Banca IFIS has decided to maintain an annual public disclosure frequency, and not using internal systems for calculating the capital requirements on credit or operational risks.

The *Pillar 3* Public Disclosure was also analysed by the Basel Committee in its January 2015 document "*Revised Pillar 3 disclosure requirements"*. This document provides indications to the supervisory bodies, who should have them incorporated into national legislation (in our case, EU) in order to enter into force. In this context, the EBA, in December 2016, published the final version of the "*EBA/GL/2016/11 - Guidelines on disclosure requirements under Part Eight of Regulation No (EU) 575/2013"* providing guidelines aimed at increasing and improving coherence and the comparability of the information to be provided in the Third Pillar. These guidelines were incorporated in the proposed draft amendment to the CRR published in November 2016. At the end of March 2017, the Basel Committee published the document "*Pillar 3 disclosure requirements - consolidated and enhanced framework*", which constitutes the second review phase of the reference legislative framework of the Public Disclosure, initiated with the above-mentioned document of January 2015. This revision aims to further promote market discipline by consolidating all the requirements already introduced and by providing a selection of the more representative indicators of the main prudential dimensions in order to support the market in data analysis, by making them more comparable. These guidelines are applicable, from 31 December 2017, only to "*Globally and Other Systemically Important Institutions*" (G-SII and O-SII), while the competent authorities may enforce other institutions to implement some or all of the guidelines contained therein. In April 2018, the Bank of Italy, taking into account the principle of proportionality, decided for Italy's less significant banks (LSI) to only request the publication of specific information on *Governance* together with the publication of the Annual Report on the financial year ending on 31 December 2018.

In May 2018, the consultation phase of the "*Pillar 3 disclosure requirements - updated framework*" document, published as a draft in February 2018 by the Basel Committee, was completed. This document represents the third revision phase of the *disclosure* requirements issued in 2004 and, in continuity with the previous revision phases, it aims to establish a single reference *framework* in terms of *disclosure*, for the purpose of harmonising market discipline. In December 2018, the final version of the document was published; the deadline for the implementation of the new disclosure obligations is set at 1 January 2022. Lastly, in the same month, the Basel Committee put out for consultation a document on proposals to change the leverage ratio and the public disclosure requirements. The consultation phase will end on 13 March 2019 with the aim of establishing the implementation of the new disclosure obligations, by 1 January 2022.

The EBA has also integrated the provisions of the aforementioned guidelines, issuing in June 2017 the "*Guidelines on LCR disclosure to complement the disclosure of liquidity risk management under Article 435 of Regulation (EU) No 575/2013*" (EBA/GL/2017/01) with additional information requirements on liquidity risk measured through the liquidity coverage ratio. The guidelines require only "*Globally and Other Systemically Important Institutions*" (G-SII and O-SII) to publish detailed quantitative information on the Liquidity Coverage Ratio (LCR); the other Banks are required to just publish the average values of a reduced number of aggregates. In this regard, Banca IFIS has included this quantitative disclosure in a simplified manner in § 1.3.3 of this document.

Then, in January 2018, the EBA issued the "*Guidelines on uniform disclosures under Article 473a of Regulation (EU) No 575/2013 as regards the transitional period for mitigating the impact of the introduction of IFRS 9 on own funds"* (EBA/GL/2018/01), which define the formats suitable for publishing information on the impacts on own funds as a result of the introduction of Regulation (EU) 2017/2395 containing "Transitional provisions aimed at mitigating the impact of the introduction of IFRS 9 on own funds". Considering that the Banca IFIS Group opted for transitional treatment with the so called "static" approach to mitigate this impact, it is also required to provide the market with information relating to the amounts of own funds, tier 1 primary capital, tier 1 capital, CET1 ratio, Tier 1 ratio, Total ratio and fully loaded Leverage ratio, as if it had not applied this transitional treatment. In this regard, Banca IFIS has included this information in § 18 of this document. Lastly, on 27 April 2018, the EBA submitted for public consultation up to 27 July 2018 the document "*Draft Guidelines on disclosure of non-performing and forborne exposures*" (EBA/CP/2018/06), which contains guidelines on the information to be provided on impaired loans and exposures subject to renegotiation. On 17 December 2018, the EBA published the definitive guidelines; the templates contained in the document will be published from 31 December 2019.

With reference to the public disclosure document, Banca IFIS provides that:

- given its relevance to the public, its shall be approved by the Board of Directors before it is distributed;
- it shall be published at least once a year together with the financial statements (art. 443 of CRR);
- it shall be subject to certification by the Chief Financial Officer pursuant to art. 154 *bis* of Italian Legislative Decree 58/1998 (Consolidated Law on Financial Intermediation).

This document has been prepared by the Bank at consolidated level and refers to its regulatory consolidation scope, which includes the holding company La Scogliera S.p.A., in accordance with applicable legislation, with the consequent recognition of minority interests in the consolidated own funds.

Further information on the Banking Group's risk profile, based on art. 434 of the CRR, is also published in the consolidated financial statements of 31 December 2018. In light of the aforementioned article, if similar information is already disclosed by two or more means, the reference is inserted in each of them and therefore the Banking Group makes use of this opportunity to complete the information by indicating the reference accordingly. For the sake of completeness, it is specified that the information relating to Own Funds and capital absorption relating to the Banking Group, effective from 31 December 2018, is contained only in this document since the new criteria provided by Bank of Italy Circular no. 262 of 22 December 2005, "The bank financial statements: schedules and rules for compilation", no longer require the publication of this information in part F of the Notes to the consolidated financial statements of the Banking Group. Further information relating to the various risk categories to which the Banking Group is exposed is indicated in part E of the Notes to the consolidated financial statements.

With particular reference to information regarding financial leverage, it should be noted that in February 2016, the Commission Implementing Regulation 2016/2002 was published in the EU Official Journal, which establishes the technical implementing standards for disclosure on the Leverage ratio, pursuant to EU Regulation 575/2013.
As of 31 December 2016, disclosure requirements regarding countercyclical capital buffer were also implemented; the disclosure therefore includes - in addition to the amount of the countercyclical capital buffer - the detail of the geographical distribution of the credit exposures relevant for the purposes of calculating the countercyclical capital buffer according to the prescribed detail. In this regard, Banca IFIS, due to the fact that it does not have significant risk exposures to countries to which a specific minimal countercyclical coefficient is assigned, with reference to the date of 31 December 2018, it is not required to make allocations to this type of capital reserve.

More information on the internal control system, on the statutory audit of the accounts and on the attestation of correspondence of accounting documents to the results of the accounting books and records by the Chief Financial Officer are present in the Report on corporate governance and on the ownership structure.

Instead, this document contains analytical information on the remuneration policies in place.

Unless otherwise specified, the data contained in the sections dedicated to quantitative information is expressed in thousands of euros. Reports without information, as they are not applicable to the Banking Group, are not published; there is also no information regarding the internal template methodologies, currently not used by the Banking Group.

The Banca IFIS Group will publish this public disclosure document and any subsequent updates on its website at the address www.bancaifis.it, in the section *Institutional Investor Relations – Risk Management.*

The Risk Management process dedicated to the preparation of this document is constantly evolving to ensure compliance with the regulatory requirements and the best practices developed by banking intermediaries, in compliance with the **principle of proportionality** on which large parts of the prudential supervisory regulations are based, considering the level and complexity of the activities performed by each intermediary, as well as the business models and risk management systems specifically used.

# 1. RISK MANAGEMENT OBJECTIVES AND POLICIES (ART. 435 CRR)

***Introduction***

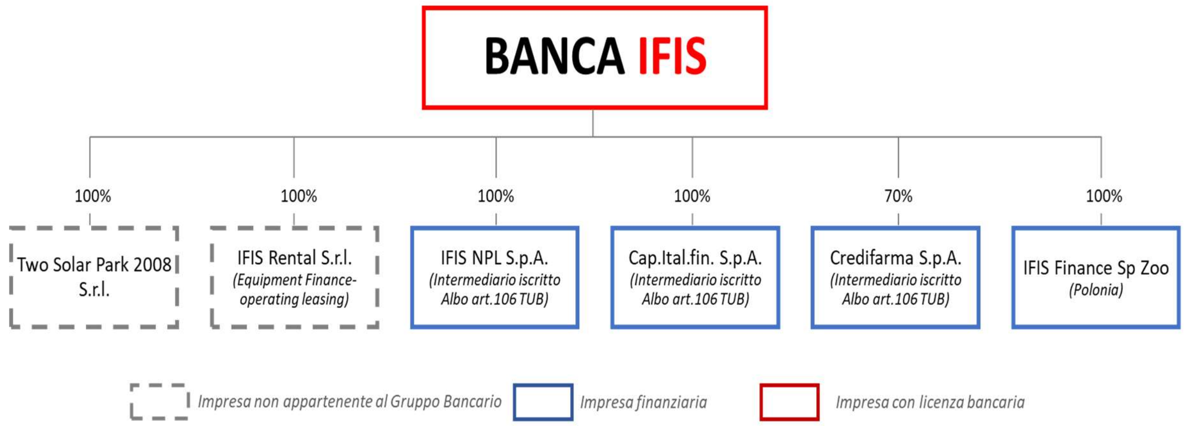
The supervisory activity is based on a system of rules and incentives allowing to pursue more effectively the objectives of a more accurate measurement of the potential risks related to banking and financial activities, and to maintain a capital structure that is more closely commensurate with the actual degree of risk exposure of each intermediary.

***The Banca IFIS Banking Group***

At 31 December 2018, the Banca IFIS Banking Group, controlled by the company La Scogliera S.p.A., following the merger by incorporation into Banca IFIS S.p.A. of the company IFIS Leasing S.p.A., which took place on 15 May 2018, and the acquisitions of Cap.Ital.Fin. S.p.A. and Credifarma S.p.A., which took place respectively on 2 February and 2 July 2018, is composed of the Parent Company Banca IFIS S.p.A. and by the subsidiaries IFIS Finance Sp. z o.o., IFIS NPL S.p.A., Cap.Ital.Fin. S.p.A. and Credifarma S.p.A.

For a complete assessment of the Group's risks, the subsidiary IFIS Rental Services S.r.l. is also taken into account. This subsidiary is excluded from the scope of the banking group and from the scope of prudential consolidation, as a non-financial company operating in the market of long-term rental of capital equipment; the company Two Solar Park 2008 S.r.l., operating in the sector of electricity production from renewable sources, is excluded from the scope of analysis. The Bank has assumed control of this company within a debt restructuring process of a credit position.

At the reference date of 31/12/2018 the Banca IFIS Group consisted of:




| BANCA IFIS | | | | | |
|---|---|---|---|---|---|
| 100%<br>Two Solar Park 2008 S.r.l. | 100%<br>IFIS Rental S.r.l.<br>(*Equipment Finance-operating leasing*) | 100%<br>IFIS NPL S.p.A.<br>(*Intermediary enrolled in the Register* | 100%<br>Cap.Ital.Fin. S.p.A.<br>(*Intermediary enrolled in the Register* | 70%<br>Credifarma S.p.A.<br>(*Intermediary enrolled in the Register* | 100%<br>IFIS Finance Sp. Z o.o.<br>(*Poland*) |

| | | | | | |
|---|---|---|---|---|---|
| | | *pursuant to art. 106 TUB/CBL)* | *pursuant to art. 106 TUB/CBL)* | *pursuant to art. 106 TUB/CBL)* | |
| *Company not belonging to the Banking Group* | | *Finance company* | | *Company with banking licence* | |

In January 2019 the acquisition of the company FBS S.p.A. was concluded. FBS S.p.A. is a financial intermediary entered on the single Register pursuant to art. 106 and operating in the sector of evaluation, management (also in the capacity of *servicer* pursuant to Italian Law 130 of 1999) and purchase of non-performing loans granted by national credit institutions.

### *Mission and corporate responsibility*

The organisational structure is divided into the following sectors:

• Business Sector;
• NPL sector;
• Governance & Services Sector.

### ***Business sector***

The Business sector includes the following business areas:

- **Trade Receivables**, dedicated to the provision of financing services to domestic businesses;
- **Pharma,** dedicated to the purchase of receivables from local health organizations and hospitals;
- **Pharmacies**, dedicated to providing financing services to domestic pharmacies;
- **International**, dedicated to providing financing services to domestic businesses engaged in export activities and to foreign companies;
- **Tax Receivables**, dedicated to the purchase of tax credits, accrued and accruing, future or which have already been claimed, mainly from companies in bankruptcy proceedings or in liquidation;
- **Corporate Banking**, dedicated to providing structured finance or investment transactions in performing non-financial companies or in shares of intermediary bodies, and evaluating the granting of new finance to Italian companies that have come or are coming from an imbalanced financial and/or capital situation;
- **Leasing,** dedicated to the provision and management of leasing products as well as long-term rental of capital equipment to small economic operators and SMEs.

### ***NPL sector***

This sector is represented by the **NPL Area**, which specialises in the purchase, management and collection of unsecured non-performing loans mainly owed by natural persons; this activity is carried out by the subsidiary IFIS NPL, which operates mainly through non-recourse purchase directly by the lenders and the management of non-performing loans.

***Governance and services sector***

This sector includes the remaining activities carried out by the Group and concerning the centralised management of services related to the governance of the Parent Company and its subsidiaries (direct funding, treasury, and operations in debt securities issued by third parties). With regard to this latter activity, Banca IFIS offers two funding products to retail customers: the *contomax* current account and the *rendimax* deposit account. The unit also provides all the wholesale banking activities and the activities carried out by the subsidiary Cap.Ital.Fin. in salary- and pension-backed loan operations.

With the goal of safeguarding its business, the Banca IFIS Group complies with the basic principles of correctness and consistency in order to achieve the best economic result while observing the Company's ethical principles and in compliance with regulations on administrative liability pursuant to Italian Legislative Decree 231/2001.

***Strategic governance, management and control bodies***

The overall risk management and control process involves, with different roles, the administrative and control bodies of the Group's companies and subsidiaries as well as the Parent Company's Management and the operational units of the entire Group.

In the model adopted by the Parent Company Banca IFIS S.p.A.:

- strategic supervision is performed by the Board of Directors;
- management is performed by the CEO, assisted by the General Manager;
- control is performed by the Board of Statutory Auditors.

The Parent Company's Board of Directors plays a crucial role in the corporate organization as it is the body responsible for determining the company guidelines and strategic objectives and for verifying their implementation, complying with industrial plans and implement strategic transactions, also by setting the principles of the direction and coordination activity of the Banca IFIS Group's companies, in the interest of the Shareholders. It carries out a supervisory function with regards to the achievement of the strategic objectives of the Bank and of the Group as a whole. In particular, concerning governance and risk controls, it is responsible for:

a) defining strategic guidelines and risk assumption, management and control with their periodic review, thanks also to an accurate, comprehensive and timely information flow system;
b) approving and periodically reviewing organisational, disclosure and risk control procedures;
c) defining and updating the roles and the responsibilities of organisational functions entrusted with the performance of company processes related to risk management;
d) guaranteeing the implementation, efficiency and effectiveness of the risk management and control system through periodical reviews and by deciding the measures to be taken to remove any deficiencies and dysfunctions that may have emerged during the risk management process.

The Board of Directors includes:

- the Control and Risks Committee, providing consulting services and support to the resolutions issued by the Board of Directors, in particular on the internal control and risk management system, as well as to the approval of the periodic financial reporting documents;
- the Appointments Committee, which provides support in appointing and co-opting Directors, as well as in the self-assessment of Corporate Bodies (Board of Directors and Chief Executive Officer). It also provides support in verifying the continued existence of the professionalism, integrity and independence requirements of company officers and in the preparation of succession plans for senior management positions;
- the Remuneration Committee, submitting proposals and providing consulting and monitoring services in the area of remuneration and incentive policies in compliance with the relevant supervisory provisions.

Management is performed by the CEO, assisted by the General Manager. The CEO is responsible for implementing the strategies and guidelines defined by the Board of Directors, to which they directly report in that regard, as well as the adoption of all the interventions necessary to ensure the adherence of the organisation and the internal control system to the principles and requirements established by the supervisory provisions, by continuously monitoring their compliance with them. For this purpose, the CEO defines the risk management, control and mitigation processes.

The Board of Statutory Auditors oversees compliance with the law, regulations and articles of association, correct administration, the adequacy of the Bank's accounting and organisational structure, and the functionality of the overall internal control system. Considering the plurality of functions and corporate structures having control tasks and responsibilities, this body is required to check the effectiveness of all the structures and functions involved in the internal control system and their adequate coordination, promoting the corrective actions for any deficiencies and irregularities detected. Due to the importance of these tasks for supervisory purposes, the Board of Statutory Auditors must immediately inform the Bank of Italy of all the facts and actions of which it becomes aware that could constitute an irregularity in the management of the Bank or a violation of the rules governing banking activity.

***Internal Control System***

The Internal Control System (hereinafter also referred to "ICS") of the Banca IFIS Group plays a central role in the corporate organisation, and has the objective of ensuring proper disclosure to the corporate bodies, and suitable supervision of all activities and, in particular, in the areas featuring greater corporate risk.

The Internal Control System consists of the set of regulations, functions, structures, resources, processes and procedures aimed at ensuring, in compliance with a sound and prudent management, the achievement of the following objectives:

- the implementation of company strategies and policies;
- the identification of tasks and responsibilities such as to ensure the separation between operating and control functions;

- risk containment within the limits set forth by the Risk Appetite Framework (RAF) for determining the Bank's risk appetite;
- the safeguard of the value of assets and protection against losses; the effectiveness and efficiency of business processes; the reliability and security of company information and IT procedures;
- the prevention of the risk that the Group is involved, even unintentionally, in illegal activities (with particular reference to those connected with money laundering, usury and terrorist financing);
- compliance of transactions with the legislation and supervisory regulations as well as with the internal policies, regulations and procedures.

The Parent Company, Banca IFIS, formalises and informs its subsidiaries of the criteria governing the different stages that constitute the risk management process. It also validates the risk management processes within the group. As regards credit risk in particular, the Parent Company sets the assessment criteria for the positions, and creates a common information base that allows the subsidiaries to know the customers' exposure to the group as well as the assessments related to the positions of the borrowers. The Parent Company decides on the adoption of the internal systems to be used for measuring risks, and determines its main characteristics, thus taking on the responsibility of carrying out the project as well as supervising the correct implementation of these systems and their constant adjustment from a methodological, organisational and procedural point of view.

The Parent Company also provides the subsidiaries with directives for creating their internal control systems. The subsidiaries must adopt an internal control system that is consistent with the strategy and the policies of the Group, in terms of controls, without prejudice to compliance with regulations applicable on an individual basis. It is, however, necessary that the Parent Company, while respecting local constraints, adopts all initiatives intended to ensure standards of control and protective measures that are comparable to those provided for by Italian supervisory regulations, including in cases where foreign legislation does not provide for similar levels of attention.

In order to verify that the Group companies conduct is in compliance with Parent Company guidelines, as well as the effectiveness of the internal control system, the Parent Company takes action so that, within the regulations' scope of application, the consolidated internal audit function periodically performs on-site checks on the Group components, taking into account the importance of the different types of risk taken on by different entities.

The internal control system is designed in compliance with the applicable regulations and the peculiarities of the business carried out by both Banca IFIS and its subsidiaries. At the date of this document, the control functions of IFIS NPL and FBS are centralised at the Parent Company, whereas for IFIS Rental Services, FBS Real Estate and IFIS Finance, with regard to the operating characteristics as well as the limited level of risk of the same for the Group, the control functions have not been established. However, IFIS Finance, in compliance with local legislation and regulatory requirements, has appointed a member of its Board as head of its anti-money laundering operations.

Regarding Cap.Ital.Fin. and Credifarma, the Internal Audit department has been centralised within the Parent Company, while an organisational structure has been established that includes the risk control unit, the unit that manages the risk of non-compliance with legislation and regulatory requirements and the anti-money laundering unit, responsibility for which has been taken by an executive currently engaged at the Parent Company, with a view to strengthening the safeguards of sound and prudent management of the intermediary.

Audits involve, with different roles, the Corporate Bodies of the Group's companies and subsidiaries, the Parent Company's Management and the Group's personnel.

Some types of audits are highlighted below:

- *line audits* – they aim to ensure that operations are carried out correctly. These audits are directly carried out by the operational structures, incorporated in procedures, or performed as part of back office operations. The operating structures are the first responsible for the risk management process: during day-to-day operations these structures must identify, measure or evaluate, monitor, mitigate and report the risks deriving from the ordinary business activity in accordance with the risk management process; they must comply with the operating limits assigned to them in line with the risk objectives and with the procedures in which the risk management process is structured;
- controls on risks and compliance (so-called "second-level controls"), with the aim of ensuring the correct implementation of the risk management process, compliance with the operating limits assigned to the various functions, and compliance of company operations to standards, including self-regulating ones;
- internal audit activities (so-called "third-level checks"), aimed at identifying violations of procedures and regulations as well as periodically assessing the completeness, adequacy, functionality (in terms of efficiency and effectiveness) and the reliability of the internal control system and of the information system. They are carried out with a set frequency in relation to the nature and intensity of the risks.

The corporate bodies promote a company culture that values the control function: all personnel, at all levels within the organisation, must be aware of the role assigned to them within the internal control system, and must be fully involved.

The roles of the various players in the internal control system (Board of Directors, Control and Risk Committee, Executive Director in charge of the internal control system, Supervisory Body pursuant to Italian Legislative Decree 231/2001, Internal Audit, Chief Financial Officer, Risk Management, Compliance, Anti-Money Laundering and Coordination function for Controlling Subsidiary Companies) are described in detail in the Report on Corporate Governance and Ownership Structures prepared in accordance with the third paragraph of art. 123 bis of Italian Legislative Decree no. 58 (TUF/CFA) of 24 February 1998 and subsequent updates, the latest version of which was approved by the Board of Directors on 7 March 2019 and published on the Bank's website in the Corporate Governance section.

Briefly, in addition to that already stated in the previous paragraph in terms of the roles and tasks performed by the administrative bodies, the roles and tasks assigned to the remaining players of the internal control system are summarised below, in particular:

- <u>Executive director in charge of the internal control system</u>: the Parent Company's Board of Directors has identified the CEO as the executive director in charge of overseeing the functioning of the internal control and risk management system. The CEO, availing himself in particular of the General Manager and of the Head of the Internal Audit Department, ensures effective management of operations and associated risks; he constantly verifies the overall functionality, effectiveness and efficiency of the Internal Control System, adjusting it if necessary; he identifies and assesses risk factors, and defines the tasks of the control units and the relevant information flows;

- Supervisory Body pursuant to Italian Legislative Decree 231/2001: Banca IFIS, sensitive to the need to ensure conditions of transparency and fairness in conducting its business, in order to safeguard its institutional role and image, the expectations of shareholders and of those who work for and with the Bank, has deemed it consistent with its corporate policies to implement the Organisational and Management Model provided for by Legislative Decree 231/2001. The Bank has thus set up the Supervisory Body, consisting of members of the Board of Directors and of the Head of the Internal Audit Department;
- Chief Financial Officer: the Parent Company's Board of Directors has identified the *Chief Financial Officer* as the figure aimed at ensuring, in line with the provisions of art. 154 bis of TUF/CFA, the reliability of the capital, economic and financial situation of the Bank and of the Group, contributing to the overall assessment of the adequacy of the internal control system on financial reporting;
- Internal Audit Department: the Internal Audit Department carries out its audit activity on both the Parent Company and the Subsidiaries, so that the main risks pertaining to said organisations are properly identified, as well as suitably measured, managed and monitored for the purpose of sound and efficient Group management. The Internal Audit Department's activity is aimed, on the one hand, at checking as part of the third line of defence, including with on-the-spot audits, the proper trend of operations and the evolution of risks and, on the other, at evaluating the completeness, adequacy, functionality and reliability of the organizational structure and of the other components of the internal control system, bringing any possible improvements to the attention of the corporate bodies of the Parent Company and of the Subsidiaries;
- Risk Management Department: the mission of the Parent Company's Risk Management Department is to (i) identify the relevant risks to which the Parent Company and Group companies are exposed; (ii) assess, measure and monitor the Group's significant risks, and (iii) guarantee a holistic and integrated view of the risks to which the group as a whole and the companies that make it up are exposed, ensuring adequate information to the governing bodies;
- Compliance Department: the mission of the Parent company's Compliance department is to oversee, according to a *risk-based* approach, the management of non-compliance risk in connection with the entire company activity, by evaluating the suitability of the internal procedures in terms of preventing the violation of external rules (laws and regulations) and self-regulation rules (for example, codes of conduct and codes of ethics) applicable to the Bank and its subsidiaries;
- Anti-Money Laundering Department: the Parent Company's Anti-Money Laundering department is called upon to continuously verify that the company procedures are consistent with the objective of preventing and combating the violation of external rules (laws and regulations) and self-regulation rules regarding money laundering and terrorist financing.

## *Organisation of the Risk Management organisational unit (Art. 435 par. 1, b)*

### *Mission of the Parent Company's Risk Management Department*

The mission of the Parent Company's Risk Management department is to:

- guarantee a holistic and integrated vision of the risks to which the Group and the Companies that are part of it are exposed while ensuring adequate reporting to the Corporate Bodies;
- identify, measure, evaluate and monitor risks that are relevant to the Group;
- ensure adequate reporting on the assumed risks to the Corporate Bodies and Committees, to the Control Functions and to the Managers of the areas subject to the risk management process;
- monitor the governance and risk management processes in accordance with the strategies and policies defined by the corporate bodies;
- guarantee an on-going development and improvement of methodologies, models, metrics and risk measurement and integration instruments;
- facilitate the transposition of supervisory regulations and directives;
- assist the Corporate Bodies in carrying out their respective tasks within the internal control system, facilitating: (i) the timely and coordinated interception of relevant information for the purpose of quantifying and managing risks; (ii) a condensed description of the corporate risks and main issues identified by the risk management system; (iii) the adoption of appropriate and timely corrective measures addressing any identified issues and priorities.

The Parent Company's Risk Management carries out its functions for Banca IFIS and, within its own management and coordination activities, it expands its scope of competence to all the companies of the Group.

### *Organisational positioning of the Parent Company's Risk Management Department*

Within the internal control system, the risk control function is part of the Risk Management Department, which reports hierarchically to the CEO. The Chief Risk Officer (CRO) has direct access to the Board of Directors and to the Board of Statutory Auditors and communicates with them with no restrictions or intermediation.

The Risk Management Department:

- is granted the authority and has the resources and expertise necessary for carrying out its tasks;
- has access to corporate data and to external data in order to appropriately manage its tasks;
- has access to all the activities of the Parent Company and of the Group companies, carried out at the head offices and at the branches, as well as to all information that is relevant for carrying out the assigned tasks, also through individual meetings with the personnel;
- has access to resources that are qualitatively and quantitatively adequate in terms of number, technical and professional skills, continuous updating, also through participation in on-going training programmes.

The Risk Management Department is separate from the Internal Audit Department and from the Compliance and Anti-Money Laundering Departments from an organisational standpoint. Moreover, it is not involved in risk assumption processes. The structures which are deemed to be involved in risk assumption, have the following characteristics (even not collectively):

- allow risk taking;
- are remunerated in proportion to business results;
- have goals that involve risk taking.

***Main activities***

The Parent Company's Risk Management Department, in fulfilling its own mission, plays a central role in governing and managing risks.

The Chief Risk Officer is the Head of this department, and, through the Chief Executive Officer, supports the Parent Company's Board of Directors in defining the Group *RAF*, the general lines of the ICAAP and ILAAP processes, the *Contingency Funding Plan*, the Group policies for the governance and management of risks and the various phases that make up the risk management process.

This department identifies the risks to which the Parent Company and Group companies are exposed and provides for the measurement and periodic monitoring of the same through specific risk indicators, planning any mitigation actions for significant risks. In this context, it ensures adequate information to the governing bodies.

The Risk Management activities are subject to periodic reporting to the corporate bodies and to the Committees through the *Tableau de Bord*, and, where required, also to the Bank of Italy, Consob and the Market. In particular, the Department guarantees the preparation, for that within its responsibility, of the group disclosures on the various regulatory (Risk Map, RAF, ICAAP and ILAAP reports, Group Contingency Funding Plan and Recovery Plan) and market (this Pillar 3 disclosure, sections E of the notes to the consolidated and individual financial statements) risk profiles.

The CRO, at the beginning of each management cycle, defines the Program of activities of the organisational units that supervises, taking into account both any deficiencies that have emerged in the checks, and any new risks. The program includes the activities to be carried out both for the Bank on an individual basis and for the Group as a whole. This document is shared with the CEO, submitted to the Control and Risk Committee and to the Board of Statutory Auditors, and approved by the Board of Directors.
At the end of each management cycle, the CRO prepares, at least annually, a Report that shows the checks performed, the results that have emerged, the weaknesses that have been detected and the proposals for actions to be taken for their removal. This report is shared with the Chief Executive Officer and subsequently sent to the Control and Risk Committee and the Board of Statutory Auditors, as well as to the Board of Directors.

The CRO reports to the Chief Executive Officer, for issues falling within its responsibility, as regards completeness, adequacy, functionality and reliability of the Group's internal control system. He promptly informs the CEO of any significant breach or deficiency found, and also supports them in the implementation of the Group RAF.

The CRO ensures the development and maintenance of methodologies, models, metrics and tools for integrated risk measurement and management. Furthermore, he oversees the process of validating the internal management models used for measuring Group risks.

The CRO supports the Parent Company's Board of Directors in defining the criteria and processes for identifying significant transactions (OMRs) and, through the organisational units that report to him, formulates preventive opinions on OMRs' consistency with the RAF; these significant transactions are subject to his assessment, during which the CRO acquires, based on the nature of the transaction, the opinion of other departments involved in the risk management process.

Furthermore, through the organisational units that report to him, the CRO:

- guarantees the monitoring of the risks arising from new products and services and those arising from entry into new business and market segments;
- guarantees the monitoring of risks arising from transactions with related parties and associated persons;
- participates in the definition of remuneration and incentive policies;
- participates in the strategic planning process with reference to aspects relating to capital requirements, prospective funding requirements and prospective assessment of Group risks;
- supports the Finance department, for the activities within his remit, in preparing the Group's periodic financial information;
- guarantees the performance of second-level controls on credit activity and, in general, to the extent applicable, on the Group's risks;
- guarantees the risk awareness process also through specific training provided to the various Group structures;
- prepares analyses and disclosures in response to specific requests from the Supervisory Authority within the scope of his responsibility.

The Risk Management unit includes three second-level units, specialised in relation to individual risk profiles ("Credit Risks", "Operational and Reputational Risks", "Financial Risks").

In June 2018, in order to improve the efficiency of the department, also in relation to the changed organisational structure of the Banking Group, in addition to the organisational units indicated above, a further three second-level organisational units were established: i) "Risk Data Governance", with the aim of developing and guaranteeing the adequacy of data quality standards on all risk areas; ii) "Model Development", with the aim of continuously developing and improving risk measurement methodologies, models and metrics; iii) "Collateral Monitoring", with the aim of overseeing the process of assessing and monitoring the value of the guarantees acquired. In redesigning the structure, in order to enhance the different skills and specific verticality of the structures, additional third-level specialist organisational units have been established in the area of credit and operational risks.

The Risk Management structure is completed by the presence of two additional organisational units that work for the *Chief Risk Officer*: i) "Risk Governance", with the task of supporting the CRO in the decision-making processes and ensuring an overall view of the various risks and their mutual interaction; ii) "Validation", which is responsible for the validation of internal risk measurement systems for management purposes.

The main objective of the aforementioned organisational units, within the scope of their activities, is:

- to provide support to the CRO in defining the Group's processes and instruments for the identification, assessment, monitoring, mitigation and reporting, linking up with the other Companies' Risk Management structures;
- to control, monitor and evaluate risk profiles, carrying out the checks and analyses defined in the relevant group policies for managing credit, financial, operational and reputational risks;
- to guarantee the development and improvement of risk measurement methodologies and models, by continuously assessing the reliability and consistency of the results;
- to collaborate in the preparation and updating of the reports and of directional and regulatory information pertaining to the Risk Management Function.

The Parent Company's Risk Management Regulation, in compliance with the Supervisory Provisions for banks pursuant to Circular no. 285/2013 of the Bank of Italy, describes in detail the scope and the mission of the same, also with reference to the management and coordination activity carried out by the Parent Company on the subsidiaries, the related organisational structure, the tasks of the staff, second-level and third-level organisational units that comprise it, the relationships that the Function maintains with the Corporate Bodies and the other organisational units of Banca IFIS as well as with the Group subsidiaries involved in the process of risk management and finally the main information flows implemented.

Group companies, where a risk control function exists, carry out independently, through dedicated organisational units, the protection and management of certain risks, in accordance with the guidelines defined by the Parent Company with regards to management and coordination activities of the subsidiaries. Specifically, the management activities relating to credit, operational, reputational, market and counterparty risk, where present, are carried out independently by the individual group companies through their Risk Management structures. This organisational solution was adopted for the subsidiaries Credifarma S.p.A. and Cap.Ital.Fin. S.p.A., whereas the risk management and control activities of the subsidiary IFIS NPL S.p.A. were centralised within the Parent Company's Risk Management function, following the results of the assessments carried out by the Parent Company on the convenience of centralising risk control activities within the same.

### *Risk profile and risk measurement and management systems (Art. 435 paragraph 1, e, f)*

The *Risk Appetite Framework* is the reference framework which governs, in line with the business model and strategic plan, the risk appetite, the thresholds of tolerance, the risk limits, and provides a single summary view of risk management policies and the reference processes that are necessary to define and implement them.

For the Banca IFIS Group, the following two categories of indicators have been defined:

- *strategic indicators:* defined by the Strategic Supervisory Body (hereinafter also OFSS from the Italian *Organismo con Funzione di Supervisione Strategica*) and necessary for the monitoring of the strategic-financial objectives of the Group, as described in this document;

- *risk indicators*: approved by the Strategic Supervisory Body, they include a set of operating limits for individual types of risks, seeking to take the process of controls over risks to a more granular level.

The categories of indicators described above are subject to regular monitoring by the Risk Management Function and are notified to both Corporate Bodies and the other business structures, based on the relevant types.

With reference to *strategic indicators*, they are divided into strategic indicators with regulatory restrictions, measured according to consolidated logics, and strategic indicators for which no regulatory restriction has been defined and are measured at the single BU or Entity level, where necessary.

For each strategic indicator relevant concepts for the purposes of RAF were defined:

- *Risk Profile* (actual risk): the actual risk assumed, measured at a particular instant in time.
- *Risk Appetite* (risk objective): the level of risk, overall and by type, which the Group intends to assume to fulfil its strategic objectives;
- *Risk Tolerance* (tolerance threshold): the maximum allowed deviation from *Risk Appetite*; the tolerance threshold is fixed in such a manner as to provide the Group with sufficient margins to operate in every case, even under stress, within the maximum risk that can be assumed;
- *Warning*: a threshold defined only for strategic indicators, free of regulatory restrictions, it is the maximum level of risk that the Group intends to assume in order to reach its strategic objectives;
- *Risk Capacity* (maximum assumable risk): a threshold defined for only the strategic indicators involving regulatory restrictions, it represents the maximum risk level that the Group is technically capable of assuming without breaching the regulatory requirements or other restrictions set by the Supervisory Authority.

| Strategic indicators | Profile | Appetite | Tolerance | Warning | Capacity |
|---|---|---|---|---|---|
| With regulatory restrictions | √ | √ | √ | | √ |
| With no regulatory restrictions | √ | √ | √ | √ | |

The *strategic indicators* are mainly attributable to:

- capital and capital adequacy;
- liquidity;
- profitability;
- asset quality;

- price.

Following a breach of the above-mentioned thresholds, an escalation process is activated which requires the timely definition of the management procedures and interventions to be activated in order to reach the tolerance threshold, after an analysis of the reasons that led to the threshold being exceeded.

***Strategies and processes for risk management***

### 1.3.1 Risk taxonomy and mapping

Banca IFIS has defined a “Risk Taxonomy” which describes the logic followed in identifying the current and/or potential risks to which the Group could be exposed in reaching its strategic objectives and, for each type, the planned prevention and mitigation instruments.

The Parent Company carries out a first identification of the risks starting with the list of minimum risks identified by the current supervisory regulations and expanding it with further significant risks which emerged from the analysis of the *business* model and the reference markets in which the various Group companies operate, of the strategic prospects, the operating methods and the characteristics of loans and sources of financing. In order to ensure greater adherence with the specific *business* models of the Group, the risks have been grouped into macro-areas.

The identification of risks and the periodic updating of the risk taxonomy are the result of a joint effort of the second-level control functions (Risk Management, Compliance, Anti-Money Laundering, Chief Financial Officer) and third-level control functions (Internal Audit), which annually meet and examine, based on the results of the previous year's risk management, the possible introduction of new risk events and/or a change in the assessment of potential risks.

The process of assessing the potential relevance of risks (so-called "inherent risk") does not take into account the possible checks or other mitigation factors that the Group has put in place.

The potential relevance of individual risks is summarised on a three-value scale (High, Medium, Low) on the basis of a joint subjective assessment of the Parent Company's control functions (so-called *judgmental* approach).

The Parent Company, for the purposes of the group processes adopted for the assessment of capital adequacy (ICAAP) and of the liquidity management and governance system (ILAAP), considers as **significant risks** the types of risk to which it has assigned the relevance levels “High” and “Medium” at the conclusion of the above risk assessment process.

The following types of risk fall within the **relevant risks**:

Credit Risk Area – within this area, the following risks are considered to be significant:

- Credit Risk;
- Concentration Risk;

Financial Risk Area – within this areas, the following risks are considered to be significant:

- Interest Rate Risk;
- Liquidity Risk;
- Risk related to the amount of encumbered assets.

Operational and Reputational Risk Area – within this area, the following risks are considered to be significant:

- Operational Risk;
- Reputational Risk;
- Model Risk.

Other types of Risk Area – the following types of risks are considered to be significant:

- Strategic Risk.

A description of the above-mentioned individual risk categories, in terms of objectives and risk management policies, is provided in the following paragraphs.

The Parent Company's Risk Management function focuses on the remaining risks, which are considered to be of "low" relevance. Please refer to the internal company regulations for the description of the risk management and control processes adopted for some of them.

The following types of risk fall into this category:

Credit Risk Area:

- Counterparty Risk;
- Country and Transfer Risk;
- Italy's Sovereign Risk;
- Residual Risk;
- Settlement and Delivery Risk;
- Risk arising from Securitisation Transactions;
- Risk arising from Investments.

Financial Risks Area:

- Market Risk;
- Credit valuation adjustment risk.

Other types of Risk Area:

- Excessive leverage risk.

### 1.3.2 Credit Risk Area

*Credit Risk*

*Credit risk is the risk of loss due to the insolvency or credit rating deterioration of the Group's counterparties and consists of the:*

- *counterparty risk – the risk of insolvency or worsening of creditworthiness of the counterparties to which the Group is exposed;*
- *transaction risk – covers both the losses that the Group sustains through non-recovery of receivables due from counterparties in default and the increasing exposure to entities who, owing to a worsening of their economic and financial situation, tend (for all cases of technical forms of credit of so-called "uncertain value") to use the credit limit allocated to them thus reducing the residual margin available.*

***Credit risk management policies and objectives***

***Objectives***

Under the guidelines approved by the Administrative Body of the Parent Company and in line with the evolution of the regulatory supervision framework, the Group pursues the objective of strengthening its competitive position in the market in relation to small-medium sized enterprises. In this context, the Group aims to expand its market share in the trade receivables areas, also in relation to subjects with specialised needs such as pharmacies, leasing, tax credit and that of doubtful loans, by providing high quality financial services, a high level of customisation, profitability and credit risk control consistent with the quality offered.

When taking into account the particular activities carried out by the Group companies, credit risk represents the most significant aspect of the overall risk assumed. The maintenance of effective credit risk management is a strategic objective for the Banca IFIS Group, pursued through the adoption of integrated tools and processes that ensure correct credit risk management in all its phases (preparation, lending, monitoring and management, intervening on problem loans).

***Organisational aspects***

Within the Banca IFIS Group, the Corporate Bodies of the Bank and of the financial subsidiaries play a fundamental role in the management and control of credit risk: according to their respective responsibilities, they ensure the adequate monitoring of credit risk by identifying the strategic guidelines, risk management and control policies, by continuously verifying their efficiency and effectiveness and by defining the tasks and responsibilities of the company functions involved in the related processes.

In the current organisational structure, specific central areas of responsibility are involved in overseeing and managing credit risk, which guarantee, through an adequate level of segregation, the execution of management activities and of first- and second-level risk controls, through the adoption of adequate IT processes and applications.

In general, the credit process as a whole, while retaining the specific features of different products / portfolios, responds to a common organisational criterion which focuses mainly on operational phases, roles, responsibilities and controls of various levels.

The organisational structure is therefore divided into the following *business units* broken down by type of activity:

- **Trade Receivables,** organisational unit dedicated to providing financing to domestic businesses;
- **Pharma**, organisational unit dedicated to the acquisition of credits claimed against local health authorities and hospitals;
- **Pharmacies**, organisational unit dedicated to providing financing to domestic pharmacies, both developed internally and reported by the sales network of the subsidiary Credifarma;
- **International**, organisational unit dedicated to providing financing to domestic businesses that carry out export activities as well as foreign businesses;
- **Tax receivables,** an organisational unit dedicated to acquiring tax receivables, mostly from companies in bankruptcy or in liquidation;
- **Corporate Finance**, organisational unit dedicated to providing structured finance or investment transactions in solvent non-financial businesses or in intermediate bodies;
- **Special Situations**, organisational unit responsible for identifying and assessing the opportunities for providing new finance to Italian companies which, although characterised by a typically managed, positive operating profitability, have exited or are exiting from a situation of financial and/or equity imbalance;
- **Leasing**, organisational unit dedicated to the provision and management of leasing products.

In the credit process, the credit activities performed by the subsidiaries also take place at the reference date of this disclosure document:

- **IFIS NPL S.p.A**., company dedicated to the acquisition, management and sale of non-performing loans, mainly originating from financial institutions and banks, resulting from the transfer of the Banca IFIS business unit dedicated to the *NPL business* completed on 1 July 2018;
- **Cap.Ital.Fin. S.p.A.**, company operating in the field of salary-backed loans and pension-backed loans, salary deductions and in the distribution of financial products such as mortgages and personal loans;
- **Credifarma S.p.A**., reference company for pharmacies for the granting of advance payments, medium- and long-term financing, equipment *leasing* and financial services;
- **IFIS Finance Sp. z o.o.**, *factoring* company operating in Poland;
- **IFIS Rental Service S.r.l**., non-regulated company specialising in the operating rental segment.

Initially, each organisational unit, in relation to its business sector, develops and manages commercial relations and *business* opportunities in collaboration with the Branches present on the national territory, and in compliance with the strategic guidelines and objectives defined by the Board of Directors.

With regard to the **credit granting** process, each *business unit* identifies the possibility of new transactions in compliance with the current credit policies and on the basis of the defined risk appetite; in this context it carries out the preliminary examination of the applications for new lending contracts and proceeds with formalising a proposal for submission to the competent decision-makers, ensuring the application of the credit policies and the established checks, and by carrying out a creditworthiness analysis as required by the internal legislation in force.

Proposals for assignment and/or acquisition of credits are presented to the competent decision-makers who, on the basis of their respective delegated powers, express their decision with regard to the granting of the loan requested; the credit decision always refers to the total exposure granted to the counterparty (or any related groups).

The branches of Banca IFIS S.p.A. do not have decision-making power in assuming credit risk; the management of the ordinary operations of customer relationships are assigned to them under the constant monitoring of the central structures and within the limits and the procedures established by the relevant Managers.

The operations of the subsidiaries provide for local decision-making limits defined within the operational and organisational scope defined by the Parent Bank Banca IFIS.

This is followed by the credit **finalisation** phase which is reflected in the stipulation of the contract, in the activities relating to the acquisition of any guarantees, in the provision of the loan granted. In these phases, the *business units* are flanked by specific organisational support units which are responsible for preparing the contract in line with the provisions of the resolution, as well as checks on the correct performance of all the activities that lead to provision of the loan.

The process of acquiring the *non-performing* loan portfolio adopted by the subsidiary IFIS NPL provides for similar organisational phases which can be summarised as follows:

- *origination*, with the identification of the counterparties with which to carry out the purchase transactions and the evaluation of the commercial interest in the execution of such transactions;
- *due diligence*, with portfolio evaluation activities carried out by highly qualified personnel, aimed at assessing the quality of the portfolio being sold, as well as the organisational impacts. Once the *due diligence* is completed, the Group sets the terms and conditions for offering/acquiring the receivables portfolio and how to manage it (judicial or non-judicial), assessing the relevant impact on operating structures;
- resolutions, with the activities necessary for the preparation of the appraisal file, the assumption, adoption and implementation of the resolution by the competent decision-maker;
- finalisation, with the preparation activities and subsequent stipulation of the purchase contract and payment of the price.

The operational management of the credit, carried out for *performing* customers, mainly includes the **ordinary management** and **monitoring** activities carried out by structures set up at each Group company in order to ensure continuous and proactive verification of assigned customers. This activity is supported by a monitoring activity carried out at Group level by a specific organisational unit set up at the Parent Company, with the aim of identifying counterparties with anomalous trends, in order to anticipate the emergence of problematic cases and to provide adequate reporting to the competent business functions.

In the event that the credit position presents objective situations of problematic repayment, it is transferred to specific functions specialised by product for the management and **recovery** of impaired transactions.

The operational management of the recovery of credits arising from the purchase of non-performing loans is handled both by internal resources of the subsidiary IFIS NPL S.p.A., and by a widespread and proven network of credit collection companies and financial agents operating throughout Italy. The company oversees the recovery operation through the courts, by liaising continually with the law firms in charge and by constantly monitoring the latter's activities in order to verify its performance and correctness of conduct. Finally, it evaluates the convenience of selling portfolios of *non-performing* loans, to be submitted - for approval - to the competent decision-making entities, in line with the assigned profitability objectives and following an analysis of the accounting, reporting, legal and operational impacts deriving from them. To this end, it makes use of the analyses made for the respective areas of competence by the relevant business functions of the Parent Company.

***Management, measurement, control and reporting systems***

Credit risk is continuously monitored with the help of procedures and tools that allow for the timely identification of positions that present particular anomalies.

The Banca IFIS Group has, over time, equipped itself with tools and procedures that enable them to assess and monitor risk specifically for each type of customer and product.

Once the assessment phase has been successfully completed and operations with the customer have begun, the credit risk is continuously **monitored**, by verifying the timeliness of repayments, the correctness of the relationship, the information reported by the System to the Central Credit Register or to selected databases and the reputational profile and to examine, for each of these, the underlying causes.

With reference to the portfolio monitoring activities, as previously reported, the receivables due from customers are monitored by specific units within the aforementioned *business units/legal entities* which are entrusted with the continuous and proactive verification of assigned customers (**first-level controls**); furthermore, there are additional monitoring activities carried out centrally by a specific organisational unit based also on the use of performance analysis models developed by the Risk Management function of the Parent Company, aimed at identifying anomalous situations in specifically identified *early warning* indicators.

Credit risk exposures to domestic companies are assigned an internal *rating* based on a model developed internally for the commercial portfolio. A project is underway which involves the evolution of the current counterparty *rating* management model towards domestic companies in consideration of the expansion of the group scope and the products offered.

Starting from January 2018, the new classification and valuation rules for financial instruments were applied for the entire Group under the new IFRS9 accounting standard.

In carrying out the measurement and control activities, the activity carried out by the Risk Management within the framework of **second-level controls** is of fundamental importance.

With reference to credit risks, the Risk Management function:

- controls, monitors and evaluates credit risks, by performing checks and analysis according to the defined guidelines; in particular: (i) evaluates the quality of credit, ensuring compliance with lending guidelines and strategies through the continuous monitoring of credit risk indicators; (ii) constantly monitors the exposure to credit risk and compliance with the operating limits assigned to the operating structures in relation to the assumption of credit risk; (iii) verifies, through second-level controls, the correct performance of monitoring on the individual exposures, in particular the impaired ones, and assesses the consistency of the classifications and the adequacy of the provisions; (iv) monitors the exposure to concentration risk and the performance of exposures classified as Large Exposures;
- carries out quantitative analysis to support the *business units* for the operational use of risk measures;
- oversees the monitoring process for the value of collateral, personal and financial guarantees acquired.

In relation to the credit risk associated with investments in bonds and *equity investments*, the Bank is constantly focused on monitoring credit quality; adequate periodic information is provided to the Board of Directors and to the Senior Management of Banca IFIS.

Within the framework of the Basel 3 principles, Banca IFIS has chosen to use the standardised method in order to determine the capital requirement against first pillar credit risks.

The Parent Company Bank IFIS, in order to assess its vulnerabilities in terms of capital and liquidity management, has developed quantitative and qualitative techniques with which it assesses its exposure to exceptional but plausible events. These analyses, defined as stress tests, assess the effects for the Bank and its subsidiaries, in terms of risk resulting from the combined movements of economic-financial variables in the event of adverse scenarios. These stress tests significantly affect credit risk.

Stress tests enable to verify the resilience of the Group, by simulating and estimating the impacts of adverse situations, and they provide important indications regarding its exposure to risks and instruments, the adequacy of the relative mitigation and control systems and the capacity to cope with unexpected losses also from a long-term planning perspective.

For regulatory purposes, the Parent Company Banca IFIS, carries out stress exercises as part of the definition of the Risk Appetite Framework, for the preparation of the Recovery Plan and the ICAAP and ILAAP reports. These are carried at least on an annual basis, as required by current prudential supervisory regulations. In this context it assesses, among others, the sustainability of credit strategies in adverse conditions.

### *Credit risk mitigation techniques*

Credit risk mitigation techniques include those instruments that contribute to the reduction of the loss that the Group would bear in the event of counterparty default; specifically, it refers to the guarantees received from customers, both collateral and personal, and any contracts that may lead to a reduction in credit risk.

In general, as part of the credit granting and management process, for certain types of credit lines, customers are encouraged to provide suitable guarantees in order to reduce their risk. They can be represented by secured guarantees on assets, such as for example pledges on financial assets, mortgages on real estate (residential / non-residential) and/or collateral securities (typically bonds) that affect a third party where the person (natural or legal) is guarantor of the debtor position of the customer in the event of insolvency.

Particularly:

- Within the *factoring* activity, when the type and/or quality of factored receivables do not fully satisfy requirements or, more generally, the invoice seller is not sufficiently creditworthy, the Bank’s established practice is to hedge the credit risk assumed by the Group by obtaining additional surety bonds from the shareholders or directors of the invoice seller. As for the account debtors in *factoring* relationships, wherever the Bank believes that the elements available to assess the account debtor do not allow to properly measure/assume the related credit risk, or the proposed amount of risk exceeds the limits identified during the debtor’s assessment, the Bank adequately hedges the risk of default of the account debtor. Guarantees issued by correspondent *factors* and/or insurance policies underwritten with specialised operators are the main hedge against non-domestic account debtors in non-recourse operations;
- within the *lending* area, according to the specificity of one’s products, adequate guarantees are acquired in relation to the counterparty's standing, the duration and the type of loan. These guarantees include mortgage guarantees, liens on plant and machinery, pledges, sureties, credit insurance and collateral deposits;
- as regards financial *leases*, it should be noted that the credit risk is mitigated by the presence of the leased asset. The Lessor maintains the ownership until the final purchase option becomes available, thus ensuring for itself a greater recovery rate in case of a default by the customer;
- in relation to transactions involving non-performing loans and the purchase of tax receivables arising from bankruptcy procedures, and the related *business* model, there are usually no actions taken to obtain coverage for credit risks;
- salary-backed loans is undoubtedly a low-risk technical form, in consideration of the peculiarities of this product which provides for compulsory insurance coverage for the risk of death and/or unemployment of the customer and the constraint, as a greater guarantee of financing, of severance indemnities accrued by the customer;
- the operation of financing to pharmacies involves an advance payment combined with a transfer or a mandate for the collection of receivables with the possibility of using the subsequent advances to reduce existing loans.

As part of the acquisition of NPL portfolios by the IFIS NPL subsidiary, there may be positions guaranteed by first-degree mortgages that present lower risk with respect to the overall portfolio acquired.

The determination of the total amount of credit that can be granted to the same customer and/or legal and economic group takes into account specific criteria for weighting the various risk categories and guarantees. In particular, prudential "differences" are applied to the estimated value of collateral guarantees, differentiated by type of guarantee.

Further information is given in § 17 of this document.

***Non-performing exposures***

The methods for classifying non-performing loans are compliant with the criteria defined by the Bank of Italy.

Non-performing exposures or those with serious problems are managed directly by specific organisational units established in each company of the Banking Group which:

- verify the willingness and ability of the counterparty to pay the debt in order to establish the most suitable recovery strategy to be adopted;
- manage litigation, both judicial and extrajudicial, related to the credit recovery;
- define and propose to the competent person, the possible amendment of the administrative status and the quantification of the "doubtful analytical results" on the assigned positions;
- ensure the monitoring of the amount of exposures classified as non-performing and the related recovery activities in progress.

Impaired assets include loans acquired by the subsidiary IFIS NPL which were purchased at significantly lower values than their nominal value; collections, usually higher than the price paid, minimise the risk of loss.

The Group, in the management of non-performing loans, defines quantitative objectives (such as maximum limits) in terms of impaired exposures as well as predefined interventions to be implemented in accordance with suitable application criteria and priorities, in order to ensure compliance with established limits over time. In managing these aspects, however, the Group must necessarily take into account the different segments of activity and related types of credit, developing solutions and actions consistent with the specificities of the individual sectors, in order to ensure the best result in terms of value protection and speed of solution.

Given the above, the Bank, when preparing the operational plan for managing the short, medium and long term NPLs, approved by the Board of Directors on 20 September 2018 and subsequently sent to the Bank of Italy, identified the following performance indicators to be pursued through careful and proactive management:

- “gross *npe ratio*”, consisting of the ratio between “gross impaired exposures” and “total loans granted to customers”;
- “net *npe ratio*”, consisting of the ratio between “impaired exposures net of the related adjustments” and the “total loans granted to customers”.

With reference to the cash credit exposures of the corporate sector outstanding on 31 December 2018 (excluding positions resulting from the purchase and management of non-performing loans of third-party originators managed by the subsidiary IFIS NPL S.p.A.), the level of the “gross NPE ratio” of the Group was equal to 9.5%, while the “net NPE ratio” was equal to 5.2%, in line with the reduction targets set for the period in question.

The pursuit of the objective to reduce the stock of medium/long-term non-performing loans, as set out in the plan, is expected to take place through a differentiated strategy in relation to the specific nature of the individual portfolios concerned (taking into consideration the type of counterparty and the specificity of individual products). In general, the actions that will be adopted are essentially attributable to the following guidelines, which have long been pursued:

- containment of the default rate in order to reduce the influx of positions to non-performing through the extension and strengthening of the monitoring activity of credit relationships aimed at anticipating, and possibly preventing, the deterioration of positions;
- improvement in “performing” repayment rates through a greater use of concession measures for counterparties showing signs of financial difficulty;
- exploitation of the expertise currently present in Banca IFIS and of the existing virtuous recovery processes in order to maximise recovery rates;
- reduction of the stock of non-performing loans through the evaluation of selective disposals of relevant individual positions, as well as through the application of current write-off policies.

More detailed information on this operation is provided in section E of the notes to the consolidated financial statements of the Banca IFIS Banking Group.

Further information is given in § 7 of this document.

### *Credit Concentration Risk*

*Risk arising from exposures to counterparties, including central counterparties, groups of connected counterparties, and counterparties operating in the same economic sector, in the same geographic region or that perform the same activity or deal with the same merchandise, as well as from the application of credit risk mitigation techniques, including, in particular, risks related to indirect exposures, such as, for example, to individual providers of guarantees.*

#### ***Concentration risk management objectives and policies***

The Banca IFIS Group pays particular attention to the concentration of credit risk with reference to all the Group’s companies, both at an individual and consolidated level. The Board of Directors of Banca IFIS has committed Top Management to take actions aimed at containing major risks. In line with the directives of the Board, those positions that are at risk and engage the Group to a considerable extent are subject to systematic monitoring.

In line with the supervisory requirements in the credit process, for the purposes of managing and controlling the concentration risk, two different phases can be distinguished: the first represented by the assignment, in particular when “large exposures” are taken on and the second is identifiable in the continuous monitoring of the quality of existing exposures, especially of higher amounts.

The Banca IFIS Group, with methods related to the nature of the products/customers handled, has adopted internal procedures consistent with the taking on and monitoring of “large exposures”, to be applied as a precautionary measure also to loans which, although not identified as “large exposures”, have dimensions such as to have significant effects on the financial soundness of the lending company in the event of a crisis of the entrusted subject/group. In particular, the Banking Group companies, relying first of all on the information provided by the Bank's database which identifies existing relationships and any legal and economic ties for all Banking Group customers, acquire during the preliminary investigation for the granting of a new loan or the monitoring of the position, all the data and information deemed necessary to evaluate the individual transaction in the overall amount of the exposure with the group to which the counterpart belongs, the composition of which is kept updated over time.

The Risk Management function periodically monitors the composition of customers and the relative degree of concentration, with particular focus on highly significant borrowers, in order to maintain, as far as possible, a satisfactory spread of credit risk and to limit potential losses in the event of insolvency of counterparties with significant debt exposures. With regard to retail portfolios, the monitoring activity on the subject of concentration is based on portfolio logics and through differentiated cases in relation to the type of product and management.

The Bank ensures constant compliance with the regulatory limits on risk concentration both on an individual and consolidated basis, as well as compliance with the most stringent regulatory limits referring to related parties. The results of the checks are reported on a quarterly basis to Top Management within the Tableau de Bord.

A quantitative representation of the “Large exposures” in place on 31 December 2018 is shown in section E of the notes to the consolidated financial statements of the Banca IFIS Banking Group. The total amount of large exposures at the weighted value on 31 December 2018 is made up of 228 million euros in tax assets, 238 million euros in exposures to equity investments not included within the prudential consolidation scope and 136 million euros in exposures to corporate customers.

In order to perform a complete measurement of the risks to which the Group is exposed, in the second pillar Banca IFIS calculates the capital add-on against the single-name and geo-sectorial concentration risk.

As is known, the single-name concentration risk aims at “correcting” and integrating the quantification of credit risk, measured with a standardised method, by defining a capital add-on that aims to cover the risk resulting from excessive concentration towards connected groups of companies. The Group measures the concentration risk relating to the “banking portfolio”, through the simplified method prescribed by Circular 285/2013 - Part One - Title III “Prudential Control Process” - Chapter 1 - Annex B, for the purpose of calculating the relative regulatory capital requirement.

A specific process is used to calculate the internal capital against geo-sectorial concentration risk in accordance with the recently revised ABI methodological proposal, which aims to provide a simplified method for determining the possible internal capital add-on based on the difference between the concentration of the corporate portfolio and that of the reference geo-sectorial benchmark portfolio. In applying the methodology, the Group uses the portfolio on a national basis as a reference as it does not have a geographical area of prevalence.

A non-negligible exposure to concentration risk can be generated by the loans granted by the Bank to counterparties classifiable as medium and large companies mainly for corporate lending and Structured Finance activities. Receivables due to the Group from counterparties belonging to retail classes and medium-sized companies - which generally refer to factoring, leasing, pharmacy, family loans, as well as to risk positions arising from the acquisition of non-performing loans - have less influence on the concentration risk given the granularity and type of exposures at risk.

### *Counterparty Risk*

*It is the risk that the counterparty to a transaction involving financial instruments defaults before the final settlement of the cash flows of the relevant transaction.*

In 2017 the Banca IFIS Group had requested and obtained authorisation to provide investment services to customers, aimed mainly at hedging the interest rate and exchange rate risks taken on by customers by offering *plain-vanilla* derivative transactions.

In 2018, the Group did not carry out activities in derivative financial products on behalf of third parties and limited its own activity to market risk hedging instruments. Banca IFIS sometimes uses financial derivatives designed to cover exposures on exchange rates.

At 31 December 2018, the Bank manages only a residual portfolio of derivative products, mainly on interest rates, resulting from transactions concluded by the former subsidiary Interbanca with leading financial institutions and corporate customers included in the trading portfolio. On the same date, some derivative contracts on exchange rates related to the management of the Bank's foreign exchange position are also present in the same portfolio. As for the transactions performed, it should be noted that the Group never undertakes speculative transactions.

At the organisational level, in the third quarter of 2018, the Proprietary Finance business unit was set up and an inter-departmental project was initiated with the aim of implementing the processes, controls and systems necessary to carry out the activity. In this respect, an impact is expected on counterparty risk arising from the activity planned for 2019 by the new business unit, which however is not considered significant in relation to the type of operations, the nature of the counterparties and the envisaged margining systems.

With regard to counterparty risk connected to repos, its monitoring consists in a precise and constant verification of the structure and quality of the securities portfolio as the underlying risk is directly connected to the creditworthiness of the counterparties with which the collateralised financing operations are carried out (generally central counterparties such as Cassa di Compensazione e Garanzia and the European Central Bank) and is proportional to the price volatility of portfolio securities provided as a guarantee. At the end of the year, there is a single repurchase agreement with a central counterparty. In consideration of the regulatory provisions regarding SFT transactions entered into with central counterparties and backed by a real guarantee on a daily basis, the impact in terms of capital requirement is in any case equal to zero.

In relation to both the low level of exposure of the derivative product portfolio and the low incidence of absorbed internal capital connected to counterparty risk (CCR) on the total absorbed internal capital on risks, it is considered that the potential relevance of the aforementioned risk at Group level is “low”.

For the measurement of counterparty risk and the measurement of its internal capital, the Bank uses the methods prescribed by Regulation (EU) no. 575/2013 of 26 June 2013 - Part Three, Title II, Chapter 6 (CCR) and for its application in Italy by Circular 285/2013, for the purposes of calculating the relevant regulatory capital requirements. In particular, for transactions involving derivatives, for the purpose of measuring counterparty risk, it applies the “market value method” (Article 274 CRR).

Further information is given in § 5 of this document.

### *Country Risk*

*It is the risk of losses caused by events that occur in a country other than Italy. The concept of country risk is broader than that of sovereign risk in that it refers to all exposures regardless of the nature of the counterparties, be they natural persons, businesses, banks or public administrations.*

Country risk represents an additional component of the risk of insolvency of individual borrowers, measured in the context of the Group's credit risk control systems.

In general, country risk derives from the possibility of loss due to events that do not depend on the solvency of the debtor, but due to the country, understood in a broad sense, in which the subject is resident. Any international loan presents a country risk, due to the fact that the debtor's repayment ability and/or possibilities can be conditioned by economic, political and social factors that transcend the micro-economic dimension of the credit relationship. In the event that the debtor is a private operator, this risk takes the form of a series of political, economic and/or technical impediments for which the public authority is ultimately responsible; if, on the other hand, the debtor identifies with the government of a country or with any other public or publicly guaranteed entity (so-called “sovereign” debtor), this risk is manifested by direct incapacity (technical, economic, financial) or refusal of these individuals to fulfil their commitments.

Most of the Banking Group's risk exposures are concentrated in Italy; the remaining exposures to non-domestic customers mainly refer to counterparties resident in the European Union. Specifically, the business operating units with significant credit exposures to foreign customers are BU International and the Polish subsidiary IFIS Finance Sp. z o.o. The target customers which BU International serves concern financing services to domestic companies that carry out export activities as well as to foreign companies, operating directly or with the collaboration of foreign correspondents. The development of relations with the latter (foreign banks or non-banking factoring intermediaries) takes place in both the import and export market mainly in the context of the worldwide Factors Chain International (FCI) company network. The subsidiary IFIS Finance Sp. z o.o. is the Group company specialised in factoring services (import/export) in the Polish market.

The evaluation of the incidence of country risk within the different operating units is of a qualitative nature and the following drivers are considered:

- the number of counterparties located in a state other than Italy with which the various operating units operate;
- the level of overall exposures for each foreign country;
- the risk that a potential event may affect the entire country, leading to the default of a large group of debtors.

In particular, in evaluating country risk for non-EU countries, information and statistics are made available by third-party institutions, such as SACE S.p.A.

With reference to exposures to foreign sovereign debtors, the Group does not present risk exposures at this time.

A quantitative representation of the geographical distribution of cash and off-balance credit exposures to customers is shown in section E of the notes to the consolidated financial statements of the Banca IFIS Banking Group. The majority of net credit exposures refer to domestic customers. In light of the above, it is considered that the potential relevance of the aforementioned risk at Group level is “low”.

### *Italy’s Sovereign Risk*

*It is the risk that the Italian government will not respect its financial obligations due to economic, financial and political factors.*

The Group is exposed for a residual part of its assets to the Italian State for investments in government securities. Consequently, possible adverse macroeconomic and/or political scenarios, which could cause the Italian Government to fail in meeting its financial obligations, would have a limited impact on the Group. As a result of the recent downgrade of Italy, at the end of 2018 the Group recorded a decrease in the value of the securities in the portfolio with modest negative impacts on equity; with reference to liquidity, the effects resulting from the decrease in the available guarantees usable for refinancing on the collateralised market are not significant.

Specific information on the Sovereign Debt is reported in section E of the notes to the consolidated financial statements of the Banca IFIS Banking Group. As of 31 December 2018, the book value of debt securities issued by the Italian Republic amounted to € 410.4 million, net of the negative valuation reserve of € 8.5 million.

The evaluation of the incidence of Italy's sovereign risk is of a qualitative nature; it is considered that the potential relevance of Italy's sovereign risk at Group level is “low”.

### *Transfer Risk*

*It is the risk that the Group, as assignor of a party that receives its main sources of income in a currency other than that of the loan, realises losses due to the debtor's difficulty in converting its currency into the currency in which the exposure is denominated.*

The transfer risk may impact on the operations generated by the Group, in particular in relation to import/export factoring, or foreign factoring abroad.

The evaluation of the incidence of transfer risk is qualitative, the driver considered is the number of counterparties that are financed with a different currency than the one in which they receive the main sources of income. As part of the lending process, in order to identify potential future losses due to the difficulty of the counterparty to convert its currency, particular attention is paid in the underwriting phase to risk factors such as the residence of the borrower, the currency of the transaction and the currency of the customer's main sources of income.

The potential relevance of the transfer risk at Group level is assessed as “low”.

### *Residual Risk*

*It is the risk that acknowledged techniques for Credit Risk Mitigation used by the Group may be less effective than expected.*

The residual risk is linked to the possibility that acknowledged techniques for credit risk mitigation used to reduce the capital requirement turn out to be less effective than expected. This generates, in the guaranteed exposures, losses greater than those covered by the corresponding capital requirements calculated by the Group in accordance with the standardised method for measuring the credit risk of the banking portfolio.

The strategies pursued by the Group require credit lines to be preferably backed by suitable guarantees and risk mitigation tools. In particular, the Bank, in relation to Corporate Finance operations, by mainly granting medium-term loans, favours transactions characterised by the acquisition of guarantees in relation to the counterparty's standing and the duration of the loan, for example mortgage guarantees, liens on plant and machinery, pledges, sureties, credit insurance and collateral deposits. In relation to subsidised finance, SMEs are financed with the support of the Guarantee Fund granted by the Ministry of Economic Development, with the dual objective of giving the company the possibility of obtaining loans without additional guarantees (and therefore without the costs of bonds or insurance policies) for the part guaranteed by the Fund, and the Bank the chance to mitigate the credit risk for the guaranteed exposure.

Similar criteria are followed by the Group's subsidiaries, based on the products they trade.

It should also be noted that, although with a non-direct impact on CRM techniques, the Group has begun to operate in the NPL sector by acquiring mortgages of varying degrees on properties[1], whose market value has a direct impact on the presumable value of credit recovery. Valuations are generally carried out by surveyors outside the Group.

The potential relevance of the residual risk at Group level is assessed as “low”.

[1] Both in IFIS NPL and in the newly acquired FBS.

Further information is given in § 17 of this document.

### *Settlement and Delivery Risk*

*It is the risk that a counterparty will not fulfil its obligation to deliver or pay in the context of a financial instrument transaction.*

The risk of settlement and delivery insists in the context of financial instrument transactions, and consequently it has the potential to affect Treasury management processes.

To evaluate the incidence of settlement and delivery risk, the bank considers the following drivers:

- the credit standing of the counterparties;
- the complexity of the financial instruments underlying the transactions;
- the percentage of significant transactions with central counterparties;
- the percentage of transactions managed through financial market infrastructures.

The potential relevance of the settlement and delivery risk at Group level is assessed as "low".

### *Risk arising from Securitisation Transactions;*

*It is the risk that the economic aspect of the securitisation transaction is not fully reflected in the risk assessment and management decisions.*

As of December 31, there are no securitisation transactions originating with the aim of achieving economic advantages with regard to the optimisation of the loan portfolio (the so-called "effective transfer of risk"). However, there is a leasing self-securitisation transaction and a trade receivable securitisation transaction originating without the transfer of risks and benefits, which are part of the more general policy of strengthening the Group's liquidity position.

The Group also has exposures to third-party securitisation transactions for small amounts and with a low risk profile, acquired for investment purposes in order to generate profit margins and to realise an appreciable medium-long term return on capital. These transactions may originate from the various business units of the Group, in relation to the characteristics of the underlying portfolio, both performing and non-performing, or in the context of liquidity investment activity.

Acquisition activities are carried out in compliance with credit risk policies and procedures, and in particular with the "Policy for the management of securitisation transactions", and in compliance with the risk appetite established within the Risk Appetite Framework. The Group invests in securitisations of which it is able to evaluate, on the basis of experience gained, the underlying related assets. In particular, the proposing unit, having identified the investment opportunity, carries out the due diligence activities in order to assess the future cash flows and the fairness of the price, coordinating, for this purpose, the relevant organisational units from time to time and formalising the related outcomes for submission to the competent decision-making body. After the acquisition, the investment is subject to continuous monitoring, with reference to the performance indicators of the underlying exposures and to the adherence of cash flows with respect to the valuations carried out at the time of acquisition.

The potential relevance of the risk arising from securitisation transactions at Group level is assessed as "low".

More detailed information on this operation is provided in section E of the notes to the consolidated financial statements of the Banca IFIS Banking Group.

Further information is given in § 14 of this document.

### *Investment Risk*

*It is the risk of a loss in value of the investment (in financial and non-financial companies) held by the Group arising from the possibility of incurring capital losses, of achieving a lower yield than expected and/or of having to sustain fixed assets for periods exceeding initial expectations. This risk includes potential conflicts of interest and inadequate organisational or corporate separation between the investment activity and the remaining banking activity.*

The investment risk is generated by transactions of a different nature, including:

- equity investment activities of industrial, commercial or service companies under development or maturity;
- additional equity investment positions arising from restructuring transactions of customers in temporary difficulty in the context of which the conversion of the debt into capital or similar equity instruments was requested;
- new investment opportunities expected in accordance with the strategic guidelines defined by the Board of Directors of the Parent Company;
- the subsidiary IFIS Rental Services S.r.l. excluded from the scope of the banking group and that of the prudential consolidation , as it is a non-financial company exercising an associated activity.

The monitoring activity of investment risk is exercised by the "Corporate Finance" business unit, which is dedicated, among other activities, to the provision of investment transactions in solvent financial companies or in intermediary bodies. In this context, it analyses the return prospects inherent in the investment and verifies the adequacy with respect to the overall risk profile, as well as evaluating whether it is worthwhile for the Bank to make the investment. Finally, it manages the operations present in the Bank's investment portfolio on an ongoing basis.

The Risk Management function oversees the monitoring or verification of compliance with regulatory limits in terms of holdings on equity investments.

The potential relevance of the risk from equity investments at Group level is assessed as "low".

Further information is given in § 12 of this document.

### 1.3.3 Financial Risks

*Interest rate risk on the banking portfolio*

*It is the risk deriving from potential changes in interest rates with reference to activities other than trading. It is the risk that unexpected changes in interest rates may cause negative effects both in income terms, reducing the interest margin, and in equity terms, reducing the economic value of the Bank.*

***Interest rate risk management policies and objectives***

The assumption of interest rate risk is an ordinary component of banking activity and can be an important source of income and capital value. However, adverse movements in market rates can have negative effects both on the level of profits and on the value of the capital of the Bank and its subsidiaries: changes in rates affect the current income level through changes in the interest margin and at the same time affect the value of the assets, liabilities and off-balance items. Therefore, an effective risk management system that maintains exposure to interest rate risk within acceptable levels is essential for the safety and financial soundness of the Group.

The interest rate risk on the banking portfolio is a transversal risk that affects all the companies of the Group and whose management is centralised at the Parent Company. The assumption of significant interest rate risks is in principle unrelated to the management of the Bank and the Group.

Exposure to this risk is analysed through the sensitivity of the interest margin and the economic value to changes in interest rates. The analyses regarding the sensitivity of the interest margin are used at management level to verify the positioning of the Group in the short term, while the economic value approach is by its nature of medium to long term relevance.

Interest rate risk monitoring uses a series of risk indicators that are verified and reported quarterly in the group's periodic reporting addressed to top management. Mitigation actions are evaluated and activated where appropriate to cover the interest rate risk on exceeding the set thresholds.

Considering the constant evolution of the Group's business model, the interest rate risk management and monitoring processes necessarily require adequate updating and/or revision phases; in this regard, during 2018, the risk positions of the acquired companies Cap.Ital.Fin. S.p.A. and Credifarma S.p.A. were integrated within the monitoring system adopted by the Parent Company, thus enabling the consequent controls and analyses to be carried out by its Risk Management function.

The assumption of interest rate risk connected to the collection activity carried out by the Treasury of the Parent Company and in line with the strategy defined by ALM & Capital Management takes place in compliance with the policies and limits set by the Board of Directors, and is governed by precise proxies on the subject that set limits of autonomy for the persons authorised to operate within the Treasury of the Bank.

The business functions responsible for ensuring the correct management of interest rate risk are: i) ALM & Capital Management, which, in line with the established risk appetite, defines the actions necessary to pursue the same, ii) the Treasury, which deals with the direct management of deposits and the bond portfolio, iii) the Risk Management function, which is responsible for proposing the risk appetite, identifying the most appropriate risk indicators and monitoring the performance of assets and liabilities in relation to the set limits, and iv) Top Management which has the specific task of proposing annually to the Board of Directors the policies for employment, collection and management of the rate risk, as well as suggesting during the year any appropriate steps to ensure the performance of activities consistent with the risk policies approved by the Bank.

For the purposes of the business assessment of capital adequacy, Class 2 banking groups, and therefore our Banca IFIS Group, are required to establish adequate measurement, control and mitigation systems to assess the interest rate risk on the banking portfolio, in terms of changes in economic value. Furthermore, from last year, the Bank of Italy requested these groups to activate new internal processes in order to carry out an assessment of the interest rate risk also in terms of changes in the interest margin or expected profits[2].

The Banking Group, for the measurement of interest rate risk relating to the "banking portfolio" for the purposes of calculating the relevant regulatory capital requirement, has been guided by the simplified method prescribed by Circular 285/2013 - Part One - Title III "Process of prudential control" - Chapter 1 - Annex C.

The Group procures mainly through retail funding, at a fixed rate for time deposits and at a non-indexed variable rate, unilaterally revisable by the Parent Company, for on-demand and on-call deposits. The Group's offer includes the option of tying up the sums for a maximum duration of up to five years. Other significant funding components are securitisation transactions mainly at a variable rate, collection from Eurosystem (TLTRO) and the issue of fixed-rate bonds (subordinated and non-subordinated) reserved for qualified investors.

The Group's assets regarding loans to customers are mainly made up of variable-rate transactions, relating to trade receivables, corporate lending and leasing. The main component of fixed-rate assets relates to the Non-Performing Loans segment and the owned securities portfolio.

During 2018, the Banca IFIS Group's exposure to interest rate risk remained at low levels and in line with the defined risk appetite values.

Further information is given in § 13 of this document.

[2] Circular no. 285 of 17 December 2013 "Supervisory Provisions for banks" - 20th update of 21 November 2017.

*Liquidity Risk*

| |
|---|
| *It arises when it is difficult or impossible for the company to fulfil its payment obligations in a timely manner due to its inability to raise funds on the market (funding liquidity risk) or to sell its assets (market liquidity risk).* |

***Liquidity risk management policies and objectives***

The liquidity risk refers to the possibility that the Group fails to service its debt obligations due to the inability to raise funds or sell enough assets on the market to address the financial deficit. The liquidity risk also refers to the inability to secure new adequate financial resources, in terms of amount and cost, to meet its operating needs and opportunities, hence forcing the Group to either slow down or stop its operations or incur excessive funding costs in order to service its obligations, significantly affecting its profitability.

In 2018, the Group continued its strategy of diversifying funding sources, mainly in order to reduce dependence on retail funding.

At 31 December 2018, the main financial sources are the capital, the on-line collection from retail customers and composed of demand and time deposits, the medium/long-term bonds issued as part of the EMTN program, the collection made at the Eurosystem (TLTRO), as well as the revolving transaction to securitise the factoring portfolio.

The Group's activities are made up of factoring operations, consisting mainly of trade receivables and at the Public Administration with maturities within the year, of medium-long term receivables, mainly coming from leasing, corporate banking, structured finance and work-out and recovery operations.

With reference to the Group’s operations concerning the NPLs and the purchases of tax receivables arising from insolvency proceedings, the characteristics of the business model imply a high level of variability concerning both the amount collected and the date of actual collection. Therefore, the timely and careful management of cash flows is particularly important. In order to ensure expected cash flows are correctly assessed, also with a view to correctly pricing the operations undertaken, the Group carefully monitors the trend in collections compared to expected flows.

The diversification strategy successfully implemented, primarily with institutional investors as of 2017, as well as the attribution of a rating by Fitch to the Group, constituted a significant step in the reduction of funding risk.

During the last period of 2018 there was a significant increase in the Group's commercial uses, fuelled both by the physiological demand that characterises the end of the year on the part of larger and more structured customers, and by structural growth by the small business in the demand for trade receivables provided by the Group. At the end of 2018, this factor generated a reduction in available liquidity reserves compared to the usual Group values recorded during 2018.

The amount of these high quality liquidity reserves (mainly held by the Group in the Bank of Italy current account) makes it possible to satisfy the regulatory and internal requirements relating to the prudent management of liquidity risk.

The Group is constantly engaged in the harmonious development of its financial resources, both in terms of size and costs, in order to have available liquidity reserves adequate for the current and future business volumes.

The business functions of the Parent Company responsible for ensuring the correct application of the liquidity policy are: i) the Treasury, which deals with the direct management of liquidity, ii) the Risk Management function, which is responsible for proposing the risk appetite, identifying the most appropriate risk indicators and monitoring their performance in relation to the set limits, and supporting iii) the activity of Top Management which has the task, with the support of ALM & Capital Management, of proposing annually to the Board of Directors the policies for funding and liquidity risk management, as well as suggesting during the year any appropriate steps to ensure the performance of activities consistent with the approved risk policies.

As part of the ongoing process of adapting liquidity risk procedures and policies and taking into account the evolution of the prudential supervisory provisions of reference, the Parent Company uses an internal framework for the governance, monitoring and management of liquidity risk at Group level.

In compliance with supervisory regulations, the Bank has also set up a Contingency Funding Plan aimed at safeguarding the Banking Group from harm or hazards deriving from a liquidity crisis and to guarantee business continuity also in the presence of serious emergency situations due to internal structures and/or market events.

Furthermore, the Risk Management function periodically reports to the Bank’s Board of Directors on the liquidity risk position.

With reference to the Polish subsidiary, the treasury activity is coordinated by the Parent Company.

More detailed information of a quantitative nature is provided in section E of the notes to the consolidated financial statements of the Banca IFIS Banking Group.

The following is the value of the LCR indicator calculated in accordance with the guidelines EBA/GL/2017/01 “on LCR disclosure to complement the disclosure of liquidity risk management under Article 435 of Regulation (EU) No 575/2013”. The figures shown refer to the simple average of the last 12 monthly observations starting from the LCR recorded at the end of 2018.

Mod. EU LIQ1

| ***Liquidity Coverage Ratio* (LCR)** | **31/12/2018**<br>(millions of euros) |
|---|---|

| | |
|---|---|
| 21 – Liquidity reserve | **1,339.7** |
| 22 - Total net cash outflows | **74.7** |
| 23 – Liquidity coverage ratio | **1,792.9%** |

## *Risk related to the portion of encumbered assets*

*The risk associated with the portion of encumbered assets derives from the unavailability of assets that can be readily liquidated through sale, sale with a repurchase agreement, guarantee assignment or securitisation.*

***Objectives and management policies of the risk connected to the quota of encumbered assets***

The risk connected to the quota of encumbered assets determines:

- the reduction in the share of assets available to creditors and unsecured depositors;
- the increase in funding and liquidity risk, as the share of assets involved reduces the possibility of obtaining new secured deposits.

The operations for which the Group normally binds part of its financial assets refer to the following:

- deposit with the Bank of Italy as a mandatory reserve;
- transactions in derivative contracts;
- time deposits given as guarantees to banks for syndicated transactions (iblor deposit);
- debt securities given as a guarantee to the Bank of Italy related to intraday advances;
- debt securities given as a guarantee to the European Central Bank for TLTRO operations;
- receivables eligible for collateralisation with the Bank of Italy through the ABACO program;
- assets used for self-securitisation transactions.

To monitor the level of exposure to this risk the Group uses the so called *"asset encumbrance ratio".*

The operational management of the risk related to the portion of encumbered assets is held by the Treasury function of the Parent Company with the support of the Financial Officing function - the ALM & Capital Management organisational unit.

To cover this type of risk, no internal capital is allocated; however, dedicated control activities are defined by the Bank's Risk Management function. These controls take the form of weekly stress tests on the value of the assets pledged as collateral for financing operations provided by the European Central Bank and designed to verify the potential impact of a detriment of the same in the context of liquidity risk.

Furthermore, within the strategic planning process and definition of the Funding Plan, the Risk Management unit measures the prospective share of encumbered assets and assesses its overall level and its sustainability with respect to the market benchmark, by subjecting them also to stress tests based on the defined scenarios.

On the basis of the final evidence, it is noted that the quota of encumbered assets remains in line with the current average values of the market.

Further information is given in § 8 of this document.

### *Market Risk*

*Market risk represents the risk of loss due to adverse movements in market prices (share prices, interest rates, foreign exchange rates, commodity prices, volatility of risk factors, and so on) in connection with the trading book for Supervisory purposes (position, settlement and concentration risks) and with the Bank's entire budget (exchange rate and position risk on commodities).*

In general, the financial risk profile of the Banca IFIS Group essentially originates from the banking portfolio, as the Group does not normally carry out trading activities on financial instruments. The activity of purchasing bonds, taking into account their classification among assets with valuation through the FVOCI method, falls within the scope of the trading portfolio and does not therefore constitute a market risk. During 2018, diversification operations of the property portfolio were carried out through the purchase of shares in UCITS (collective investment funds) funds, the underlying of which mainly concerns bonds with short-term duration. This type of investment is evaluated using the FVTPL method.

The only activity that can generate market risks is attributable to foreign currency positions subject to exchange rate risk and derivative contracts.

In relation to exchange rate risk, currency transactions mainly consist of:

- transactions entered into with customers normally related to typical factoring and lending activity, for which the exchange risk is mitigated from the outset by resorting to funding with the same original currency;
- transactions that are part of the typical Treasury activity for the management of mismatching between use by customers and the related currency procurement carried out on the market.

In this context, the Treasury function has put in place some derivative contracts on exchange rates linked to the management of the Bank's foreign exchange position. The classification of these derivatives as financial assets or liabilities held for trading is not an expression of the purpose of the transaction, the objective of which is to mitigate the effect of possible fluctuations in the exchange rates of reference.

In relation to transactions in derivative contracts, in line with internal policies that do not allow for any type of transaction for speculative purposes, at the end of 2018 the trading portfolio was composed of residual transactions resulting from the Corporate Desk activity carried out by the former Interbanca S.p.A. and ceased in 2009, in which derivative contracts were offered to customers to cover the financial risks assumed by the latter; all outstanding transactions are covered, for the purpose of cancelling market risk, with back-to-back transactions, in which external market counterparties have assumed an opposite position to that sold to corporate customers. The risk of this portfolio is therefore to be considered intangible, also from a future perspective.

For measuring market risks in the trading portfolio for supervisory purposes and for measuring exchange rate risk, the Bank follows the methods prescribed by Regulation (EU) no. 575/2013 of 26 June 2013 - Part Three, Title IV, and Circular 285/2013 for its application in Italy, for the calculation of the relevant regulatory capital requirement.

In particular, the standardised methodology makes it possible to calculate the total capital requirement, based on the so-called "building-block approach", according to which the overall requirement is obtained as the sum of the capital requirements against the following risks:

- position risk which expresses the risk that derives from the fluctuation of the price of securities for factors relating to the performance of the markets and the situation of the issuing company; in this context, it takes into account, where present, the basic risk which expresses the risk of losses caused by non-aligned changes in the values of opposite positions, which are similar but not identical;
- settlement risk which expresses the risk of loss resulting from the failure to settle transactions in debt securities, equity securities, derivative contracts, currencies and commodities;
- concentration risk which represents any additional capital cover required in the event of temporarily exceeding the individual credit limit as a result of risk positions relating to the trading portfolio;
- exchange rate risk is the risk of incurring losses due to adverse changes in the prices of foreign currencies on the positions held, regardless of the allocation portfolio (trading portfolio for supervisory purposes and trading portfolio).

The Bank, with reference to the contained positions belonging to the trading portfolio for supervisory purposes, essentially measured the position risk.

The market risk positioning is periodically reported to the Board of Directors, within the quarterly Tableau de Bord prepared by Risk Management.

In light of the above, the potential relevance of market risks at Group level is considered to be "low".

Further information is given on § **Errore. L'origine riferimento non è stata trovata.** of this document.

*Credit valuation adjustment risk*

*This risks refers to an interim market valuation adjustment of the portfolio of transactions with a counterparty, referring to OTC derivatives. This adjustment reflects the current market value of the entity's counterparty risk but it does not reflect the current market value of the entity's credit risk in relation to the counterparty.*

The credit valuation adjustment risk (CVA) insists on the same portfolio exposed to the previous counterparty risk analysed (see § 1.3.2); it reflects the current market value of the risk itself.

For the measurement of credit valuation adjustment risks and its internal capital, the Bank follows the method prescribed by Regulation (EU) no. 575/2013 of 26 June 2013 - Part Three, Title VI and Circular 285/2013 for its application in Italy, for the purposes of calculating the relevant regulatory capital requirement. In particular, for transactions involving derivatives, it adopts the “standardised method” (article 384 CRR) in order to measure the credit valuation adjustment risk.

In relation to both the low level of exposure of the derivative product portfolio and the low incidence of internal capital absorbed connected to the credit valuation adjustment risk (CVA) on the total internal capital absorbed on the risks, the potential relevance of the aforementioned risk at Group level is considered to be “low”.

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### 1.3.4 Reputational and Operational Risks

*Operational Risk*

*Operational risk is the risk of losses arising from inadequate or dysfunctional procedures, human resources, internal systems or external events. The definition includes, among other things, fraud, human errors, business interruptions, unavailability of the systems, contractual defaults, and natural disaster. Different types of risks fall within the definition of operational risk and, based on their significance for the Group, are measured separately.*

***Objectives and management policies of operational risk***

In compliance with legislative provisions and the best practices in the sector, the Banca IFIS Group has already defined the overall framework for the management of operational risks. This framework consists of a set of rules, procedures, human, technological and organisational resources and control activities aimed at identifying, measuring, monitoring, preventing or mitigating, as well as communicating to the appropriate hierarchical levels, the operational risks assumed or assumable in the various organisational units. The key processes for the correct management of operational risk are also represented by loss data collection (LDC) and the forward-looking self-assessment of exposure to operational risk (Risk Self-Assessment - RSA). In addition, another fundamental item of the operational risk governance and management process is represented by the adequate training of resources. Indeed, the Banca IFIS Group is constantly committed to the professional training and growth of its human resources.

The operational risk monitoring aims at ensuring a continuous control of the exposure to this type of risk and is carried out through:

- The analysis of the evidence resulting from the Risk Self-Assessment and Loss Data Collection activities; in the event that the findings should reveal significant criticalities, the appropriate remediation actions are identified, shared and subsequently planned with the various responsible operating units that are affected;
- the definition and calculation of specific risk indicators and the periodic verification of compliance with the relative monitoring thresholds (these indicators are reported quarterly in the periodic reporting to the corporate bodies or in specific reports addressed to the structures concerned).

In particular, risk indicators are characterised by the following:

- the presence of alert/alarm thresholds;
- being comparable with historical time series.

Considering the development of the business and the internal and external operating context in which the Group operates, the indicators are subject to a periodical update/review in order to identify any changes in the risk scope.

In this regard, during the 2018 financial year, in relation to the acquisition, merger and demerger operations of the various subsidiary companies, the structured process of data collection of the losses arising from operational risk events was further consolidated through a constant and continuous activity, by the Risk Management function, for disseminating a culture among the business structures aimed at the proactive management of operational risks and therefore raising awareness of the related Loss Data Collection process. For relevance, the methods for managing and monitoring operational risks have been standardised at Group level, also extending the tools developed and used at the Parent Company to the new corporate scope. In this context: (i) the tool dedicated to the collection of loss events - RiskOp - was updated in order to make it usable by all Group companies; (ii) within the various operating units of the subsidiaries, the names of persons who perform the role of Risk Champion have been identified, as being responsible for the timely and complete reporting of operational (and reputational) risk events that occur during the performance of different business processes and for these figures; (iii) suitable training was provided; (iv) a monthly monitoring activity was started on a common set of Key Risk Indicators, to be carried out both at individual company level and at Group level, in order to be able to continuously detect any critical issues that may arise. Finally, in the fourth quarter of 2018, Risk Self-Assessment campaigns were launched for operational (and reputational) risk, adopting the methods defined at Group level that enable a homogeneous assessment of future risks.

The operational risk mitigation phase takes place in the form of identification and implementation measures aimed at preventing and mitigating exposure to operational risk (through corrective initiatives or adaptation of processes, systems, etc.) or risk transfer interventions (through the stipulation of insurance policies). In particular, mitigation activities are carried out for the purpose of identifying specific areas of vulnerability based on an analysis of evidence resulting from the LDC and RSA activities, or following a breach of the pre-set thresholds for risk indicators; these phases can be summarised as follows:

- review and share the proposals for corrective actions applicable to corporate processes with a significant level of operational risk;
- define an implementation plan of proposed actions, setting up priorities, execution times and resources involved;
- rationalise and optimise the mitigation actions in terms of costs/benefits;
- verify, on an on-going basis, the progress and efficacy of the undertaken actions.

In relation to the companies of the Banca IFIS Group, we specify that the management of operational risk is, at present, ensured by the close involvement of the Parent Company which takes decisions in relation to risk management strategies and the overall management framework for operational risk has been integrated, as previously reported, in the acquired companies. The functions which are primarily responsible for setting up adequate operational risk controls are the Organisational units, which are responsible for defining and adjusting the organisational structures and company processes over time, as well as the ICT unit, which is responsible for corrective or evolutionary interventions on the applications used. It is the responsibility of the individual operational structures to directly control operational risk (line controls); further controls are entrusted to second level control functions and in particular to the Risk Management Department which includes professionals dedicated to monitoring operational risks.

Various types of risks fall within the scope of operational risks. In this regard, the following are noted:

- the risk of fraud understood as the risk of incurring economic and reputational losses due to fraudulent acts; both internal and external frauds are included[3]. In order to prevent the risk of fraud, the Risk Management function continuously assesses the processes, identifying weaknesses and implementing specific line controls aimed at identifying the so-called “anti-fraud red flags” (fraud risk indicators) and creates new ones if necessary; this activity is supported by the use of databases (Cerved, Crif, Assilea) and dedicated IT tools (Scipafi, detection fraud systems related to payment instruments). The risk mitigation activity is completed through the provision of specific Anti-fraud training to the different operating structures. In this context, a survey, study and analysis of cases of fraud suffered are also carried out;
- IT risk, that is the risk of incurring economic, reputational and market share losses in relation to the use of information and communication technology. The IT risk is assessed through a proprietary method, which involves carrying out an analysis of the IT services provided by the Group and any outsourcers with regard to: (i) the estimate of the value, on business processes, of a possible disruption of the IT Service in question and (ii) the estimate of the susceptibility to damage, understood as the potential exposure to threats. The methodology, in particular, provides for the risk classification of the individual IT service on a scale of ordinal values to ten classes; in accordance with the resulting level of risk it is then possible to identify and define the priority of any remediation actions to be implemented. Regarding the risk of business continuity, the Group currently has several Business Continuity Plans, developed for the various subsidiaries, which include the respective Disaster Recovery plans. Each year, operational continuity and disaster recovery tests are performed by simulating service interruptions and by activating the same interrupted applications on other sites;
- the risk of non-compliance, that is the risk of incurring legal or administrative sanctions, significant financial losses or reputational damage as a result of violations of mandatory rules (of law or regulations) or of self-regulation. In this regard, the Group has adopted a qualitative methodology for assessing this risk, which specifically includes: i) the performance of compliance checks, according to a risk-based approach, which enables to assess the completeness and adequacy of the processes as well as the functionality and reliability of the safeguards put in place in order to guarantee the correct management of the risk of non-compliance; ii) the performance of continuous checks by which the effectiveness of the safeguards in place is tested; iii) updates to the continuous controls map, which are made in order to include additional controls aimed at examining the identified and/or requested controls as part of their own verifications. The Compliance function, in accordance with a risk-based approach, supervises the management of the risk of non-compliance with regard to the entire activity of the Group;
- the risk of money laundering and terrorism financing, that is the risk of involvement, even unconsciously, of the Group in money laundering and terrorism financing activities. In this regard, the Group carries out a risk self-assessment exercise in line with the

[3] Internal fraud means all fraudulent events carried out maliciously and deliberately by an entity within the Banca IFIS Group, also with the collaboration of external parties, for personal gain (not only of an economic nature) or in favour of third parties and which result in damage to the Group, for customers or for third parties for which the Group is responsible. External fraud, on the other hand, means events of fraud, theft or embezzlement, carried out by external parties for personal gain and which result in damage to the Group, customers or third parties for which the Group is responsible.

provisions of art. 15 of Italian Legislative Decree 231/2007 inspired by the principles set out in the document issued by the Bank of Italy on 16 October 2015 and the guidelines issued by FATF in October 2014 "Risk-based Approach Guidance for the Banking Sector". This self-assessment exercise is based on a qualitative-quantitative methodology aimed at identifying the potential level of risk exposure as well as measuring the vulnerability of the existing safeguard systems. The Anti-money laundering function is responsible for managing the risk of money laundering and terrorism financing on behalf of the Group;

- the risk of incorrect financial reporting, understood as a voluntary or involuntary action potentially generating errors in the Group's financial statements. The internally developed assessment process is inspired by the principles and guidelines defined by the *Internal Control – Integrated Framework* issued by the *Committee of Sponsoring Organizations of the Treadway Commission* (known as CoSO) and by the *Control Objectives for Information and related Technology* (known like CobiT), considered as reference models accepted internationally. The analyses carried out are aimed at identifying and mitigating the main risks to which the company is exposed in the execution of the relevant transactions which generate the information contained in the financial statements and in general in any other information of a financial nature. The Financial Reporting and Monitoring function is responsible for the setting up and monitoring of adequate safeguards.

Risks relating to IT, non-compliance, money-laundering and terrorism financing, incorrect financial reporting, are assessed and represented separately through dedicated qualitative assessments, defined by the respective competent units. With regard to fraud risk, this is assessed within the broader operational risk management process; however, given the peculiarity of this risk as described above, dedicated prevention and detection activities are provided for within the Bank's Risk Management function.

For the measurement of operational risk and of internal capital, the Banking Group, in consideration of the size and the limited operational complexity, has followed the "basic method" governed by Regulation (EU) no. 575/2013 of 26 June 2013 – Part Three, Title III and Circular 285/2013 for its application in Italy, for the purpose of calculating the regulatory capital requirement. In particular, it calculates the mandatory minimum capital requirement for operational risks by using the Basic Indicator Approach (BIA). This method quantifies capital absorption to the amount of 15% of the average of the last three financial years of "relevant indicator" values referred to in art. 316, Regulation (EU) no. 575/2013 of 26 June 2013, which are representative of the company operating volumes.

Further information is given in § 11 of this document.

### *Model Risk*

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|---|
| It represents the possibility that there are economic and/or capital impacts resulting from the development and implementation of any model, proprietary or not, by the Group and by the improper or incorrect use of the results produced by the models used. |

#### ***Objectives and model risk management policies***

A model can be defined as "*a system, a quantitative methodology or an approach that applies statistical, economic, financial techniques or mathematical theories and assumptions in order to process input data and obtain quantitative estimates*"[4]. A model consists of three components:

- starting information, which results in input data, hypotheses and assumptions;
- the process, through which the inputs are transformed into estimates;
- reporting, which converts the estimates into information useful for the business in question.

According to the Banca IFIS Group, the model risk involves the use of internal models even if used exclusively for management purposes. In particular, by order of relevance, we refer to the models that can be used by the Bank and/or the Group for the valuation of balance sheet items, the calculation of capital requirements and the parameters related to the quantification of the liquidity position for strategic plans and business plans.

Model risk monitoring takes place through a diversified set of analyses and checks carried out in different phases, aimed at certifying the various valuation methods used by the Banca IFIS Group, in order to monitor the reliability of the models, their limitations and weaknesses, the possible distortions resulting from their use over time, the possible deterioration of their performance and, therefore, to direct the corrective actions to be implemented.

During 2018, the analysis and drafting of the model risk management policy was started, as well as the related management process which initially provided for a survey of the existing models and subsequently the assessment and mitigation of the risk related to them. In 2019, this policy is also expected to be applied to the subsidiaries.

To cover this type of risk, no internal capital is allocated, however dedicated controls are defined, carried out by the Validation function, for which the *Chief Risk Officer* is responsible.

## *Reputational Risk*

| |
|---|
| *This is the current or prospective risk of a decline in profits or capital as a result of a negative perception of the Bank's reputation by customers, counterparties, Bank shareholders, investors or Supervisory Authorities.* |

***Objectives and reputational risk management policies***

Reputational risk is a transversal risk that impacts all those entities of the Group which, due to their operations, have relations with external entities. Reputational risk is considered a second-level risk, as it is generated by the occurrence of other types of risk, such as the risk of non-compliance, strategic risk and in particular, operational risks.

[4] See "*Supervisory guidance on model risk management*" published in 2011 by the *Board of Governors of the Federal Reserve System* and by the *Office of the Controller of the Currencies*.

The Group has focused its attention on the operational areas that can be deemed by stakeholders as negative evaluation elements.

In particular, the following risk management drivers have been identified:

- customer relationships: enhancement of relations with customers in terms of reputation, economic strength, efficiency and courtesy in providing quality services in line with their expectations;
- relationships with counterparties involved in financial transactions: relations with counterparties shall be characterised by correctness, transparency and compliance with the contractual obligations;
- social and ethical responsibilities: pursuit of growth objectives of a social and ethical nature;
- compliance with legislation: actions aimed at ensuring compliance with laws and regulations and its timely updating;
- human resources: activities aimed at preventing fraudulent behaviour, staff errors and non-compliance with the rules relating to the employment relationship.

The organisational structures that interact with stakeholders collect information and report the factors that can have negative reputational impacts.

Development dynamics and characteristics of online collection represent a high reputational risk in terms of retail customer deposits.

The large number of borrowers related to operations in the Distressed Retail Loans segment and the involvement of parties outside the Group for recovery activities are potentially relevant factors in terms of reputation.

In addition, the Lease segment uses a network of external agents for business development, which may also harm the Group's reputation.

Ultimately, this risk also becomes relevant with regard to bank counterparties as sources of financing, even if effectively mitigated by the development of direct operating relations and by the professional nature of the counterparties themselves, as well as by the Bank's growing diversification of sources of funding.

The Group has defined and adopted an overall framework for the governance and management of the reputational risk, divided into the following phases:

- identification of the threats to reputation which affect the operations carried out by the Group;
- assessment and monitoring of exposure to reputational risk by: (i) conducting a periodic risk self-assessment exercise; (ii) defining and calculating specific risk indicators as well as checking compliance with their monitoring thresholds; (iii) the audit, in the context of the Loss Data Collection activity of the operational risk management process, of any reputational effects resulting from operational risk events;
- reputational risk mitigation through the identification and execution of corrective interventions or adjustments aimed at preventing and mitigating exposure to reputational risk;

- implementation of periodical information flows aimed at collecting and reporting any evidence resulting from the activities provided for by the reputational risk management process.

In particular, the Risk Self-Assessment methodology in terms of reputational risk is based on the identification of the list of threats to reputation, starting from the operational risks present in the RSA; these threats are then evaluated at individual organisational unit level, in order to trace:

- the reputational impact, that is the reputational consequences that may occur;
- the frequency, intended in terms of number of probabilities that the potential threat to reputation actually occurs;
- current checks or the level of mitigation present.

The assessment process leads to a summary judgement related to reputational risk expressed on an ordinal scale. Internal capital is not allocated to cover this type of risk.

In terms of reputational risk, the Risk Management function is constantly and continuously carrying out activities such as disseminating a culture among the corporate structures aimed at the proactive management of risk and therefore raising awareness to promptly detect any critical issues that may arise in the various areas of the Group's operations. During the 2018 financial year, in relation to the business evolutions of the Group, similar activities were carried out at the subsidiaries. Finally, in the fourth quarter of 2018, the Risk Self-Assessment campaign was launched for reputational risk, adopting the new methods defined at Group level which enable a homogeneous assessment of future risks.

### 1.3.5 Other risk areas

*Strategic Risk*

*It is the current or future risk of a decline in profits or capital as a result of changes in the operating context or inappropriate management decisions, inadequate implementation of decisions or lack of responsiveness to changes in the competitive environment.*

***Objectives and strategic risk management policies***

Strategic risk is of particular importance in the process of assessing the sustainability of the Group's business model; it is considered a significant risk.

As specified in the document "Group Policy for Strategic Planning", the definition of the Group's overall business model and the identification of business strategies are the responsibility of the Board of Directors and the Chief Executive Officer of the Parent Company.

Following a process of sharing with the General Manager and the Heads of the various operating units, Strategic Planning prepares the Strategic Plan containing the strategic objectives defined by the Board of Directors, and assesses the risks and sustainability in terms of capital resources. In addition, the Board of Directors assesses the implementation risk, that is the degree of vulnerability of the corporate strategy and of the Group's capital position.

Strategic risk management is therefore the responsibility of the Management and Strategic Supervisory Bodies of the Parent Company. The Strategic Supervisory Body of each individual Group company, as part of the Group's strategic planning process, having made the appropriate assessments for the best protection of the company's interests and within the scope of the prescriptions received, implements the Group Strategic Plan and the Group business model, with particular reference to the component for which it is responsible.

The Parent Company's Risk Management function supports the corporate bodies in assessing the sustainability of business strategies and the impact of strategic risk through appropriate safeguards, such as:

- monitoring the objectives set out by the strategic plan, which regularly updates the development guidelines in relation to the progress of management;
- the ongoing verification of the capital sustainability of the strategic plan, through the monitoring of strategic indicators and the related thresholds for risk appetite, risk tolerance, alert thresholds and risk capacity;
- verification of the profitability at risk of the capital invested.

The verification and the quarterly reporting of the company positioning with reference to the identified indicators is integrated in the periodic reporting system for top management (*Tableau de Bord*).

Internal capital is not allocated to cover this type of risk.

### *Excessive leverage risk*

*The risk that a particularly high level of indebtedness compared to the level of own funds would make the Group vulnerable and would make it necessary to adopt corrective measures to its business plan. This would include the sale of assets with the recognition of losses that may involve value adjustments also to the remaining assets.*

Excessive financial leverage risk impacts the Group across the board and the assessment of the incidence of this risk is purely qualitative.

Leverage risk is subject to quantitative limits: there is no provision for a first pillar capital requirement, nor does the risk contribute to the definition of the total internal capital. The risk is monitored quarterly by calculating the leverage ratio indicator in line with the regulatory indicator and calculated as the ratio between Tier 1 capital and a measure of the overall exposure which includes on-balance sheet and off-balance sheet items not deducted.

Financial leverage risk is included in the RAF and therefore is subject to the procedures and control mechanisms envisaged therein. Leverage Ratio is one of the Key Risk Indicators monitored within the RAF for 2018; during 2018 it was approximately three times higher than the minimum EBA value of 3% coinciding with the Risk Capacity defined in the RAF.

The potential relevance of the financial leverage risk at Group level is assessed as “low”.

Further information is given in § 16 of this document.

### 1.3.6 Monitoring and Reporting

Monitoring the risk objectives aims at identifying any criticality of the moments of corporate planning and management of the risks and is preparatory to the implementation of corrective and realignment actions, in compliance with the general principles of sound and prudent management.

This activity is managed by the Risk Management department that has the task of ensuring protection and the integrated management of risks by ensuring the development and improvement of measurement methods and models.

The Risk Management function, assisted by specialist organisational units and other organisational control units, produces periodic reports to the Bodies and business units in order to allow verification of the consistency between the implementation of the RAF, the strategic objectives and the approved thresholds (see the section on reporting flows).

Relevant update documents, among others, are drawn up annually: (i) to determine the Group's risk appetite (Risk Appetite Framework – RAF); (ii) to assess the capital adequacy (Internal Capital Adequacy Assessment Process – ICAAP) and liquidity (Internal Liquidity Adequacy Assessment Process – ILAAP); (iii) for the emergency plan to deal with contingency funding and for promptly covering liquidity shortfalls (Contingency Funding and Recovery Plan – CFRP).

The Group Recovery Plan was also drafted in 2018, a document containing the preparatory measures aimed at preventing and promptly resolving any crisis situations; it describes the ways in which the Group intends to restore a condition of capital and financial balance in when it is near to default. In September 2018, the Risk Management function collaborated in the preparation of the operational plan for managing the short-, medium- and long-term NPLs, subsequently approved by the Board of Directors and sent to the Bank of Italy. The plan defined the set goals to reduce the impaired exposures for the three-year period 2019-2021, and the actions to be taken to achieve them, as well as an illustration of the assessments underlying the strategies and the identified objectives.

In addition, on a quarterly basis, the Risk Management function prepares suitable reports for the Board of Directors (*Tableau de Bord*), which enables monitoring not only of strategic indicators but also of management risk indicators. Lastly, a detailed periodic report is also prepared to support the Group's business structures.

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### *System of Governance (Art. 435, paragraph 2)*

Pursuant to the Articles of Association, the Parent Company's Board of Directors is composed of five to fifteen members, elected by the Shareholders' Meeting. Their term of office shall last for a period not exceeding three years, as established upon their appointment, and it shall end on the date of the Shareholders' Meeting convened to approve the financial statements for their last year of office.

The appointment of the members of Banca IFIS Board of Directors is based on lists submitted by shareholders, according to Article 11 of the Articles of Association. The aforementioned article also provides that the number of candidates indicated in the lists and belonging to the least represented gender must be at least one third (with the exception of the lists that present a number of less than three candidates) and that persons that do not meet the requirements of integrity, professionalism and independence as established by art. 26 of Italian Legislative Decree no. 385/1993 cannot be included.

Before the appointment, the Parent Company's Board of Directors, supported by the Appointments Committee, defines the best qualitative and quantitative composition for the body to perform its functions; the detailed ideal composition is brought to the attention of the Bank's shareholders, so that the choice of candidates to be presented takes into account the professionalism and expertise required; the relevant document "Best quantitative and qualitative composition of Banca IFIS's Board of Directors" is published on the Bank's website.

After the appointment, the Board, in compliance with the Supervisory Instructions for banks (Title II, Chapter 2, sections I and II) and within thirty days of the appointment, verifies that each of its members possesses the requirements of professionalism and integrity pursuant to articles 1, 3, 4 and 5 of the Italian Ministerial Decree 161/98, verifies the non-existence of grounds for suspension pursuant to art. 6 of the same Italian Ministerial Decree 161/98 as well as the absence of appointments in competing companies or groups of companies.

Furthermore, following appointment and in accordance with the provisions of Borsa Italiana's Corporate Governance Code, the Board performs the necessary checks in order to verify compliance with the independence requirements for a minimum number of directors of at least a quarter of the total number of board members.

The Board also verifies annually the suitability of its members to perform the functions attributed to the body in terms of professionalism, integrity and independence, as part of the self-assessment process required by Bank of Italy Circular no. 285/2013 (Title IV, Chapter 1). It also aims to verify the correct and effective functioning of the body and its adequate composition, by identifying the main weaknesses, promoting discussion within the Body and defining corrective actions to be adopted, as well as strengthening cooperation and trust between the individual members.

The Board's best qualitative and quantitative composition (9 Directors, 4 of whom are independent and at least 3 are women) was submitted to the Shareholders in view of the Shareholders' Meeting that on 22 March 2016 appointed the Board of Directors for the three year period 2016-2018.

The Board in charge underwent the self-assessment process for the 2018 financial year and, at the meeting of 18 January 2019, approved the related Report, which revealed a qualitative and quantitative composition of the Body which was adequate in terms of gender diversification (the female component has gone from 2 to 3 compared to the previous mandate) and role assigned to directors (the number of independent directors has increased from 3 to 4). It was also adequate for the complexity and activities of the Body and in line with the current guidelines that favour a composition of the same that is non-excessive and with an adequate degree of heterogeneity to enable the directors to make an effective contribution to the activities of the Board.

An appropriate degree of diversification in terms of gender, in addition to age and geographical origin, favours a diversity of approaches and perspectives in analysing problems and in decision-making, avoiding the risk of behaviours of mere alignment with prevailing positions, both internal and external to the Bank.

In this respect, the selection process of Board members adopted by the Bank protects and promotes member diversity from the time of appointment, since the list voting system governed by the Articles of Association guarantees the presence of at least one director appointed by minority shareholders and compliance with the regulations on the number of candidates belonging to the gender that is less represented.

In addition, the member selection process ensures the Board's heterogeneity, identifying within the body an adequate degree of diversification, also in terms of expertise, which shall be widespread and diversified both under the managerial profile and the technical profile (legal, accounting, tax, financial, risk management and control, corporate governance, IT processes, business organization and human resources areas).

In order to ensure a profitable internal comparison and to contribute to decision-taking in accordance with the interests of the Bank, additional specific skills and experiences are disseminated within the Board of Directors, which are attributable to the multiple types of operations of the Bank (for example to the activities in the field of non-performing loans, factoring and tax credit).

As a matter of fact, performance of the functions assigned to the strategic supervision body requires the presence of persons who:

- Are fully aware of the powers and obligations inherent to the roles they are each called upon to carry out (executive and non-executive duties, independent members, etc.);
- have a level of professional skill that is appropriate for the role, including with regard to the Board's internal committees, and adjusted to the operating characteristics and size of the bank;
- have skills that are different from yet complementary to those of the other members, in order to ensure that each member contributes, with the other members, within committees they are a part of and in collective decisions, to identify and pursue suitable strategies and to assure effective risk management in all areas of the Bank;
- Dedicate the necessary time and resources to their office - limits to the number of positions possible to hold remaining firm;
- focus their actions on pursuing the overall interests of the bank, regardless of the corporate structure that voted for them or the list from which they are taken;
- guarantee compliance with operation and judgement independence.

Further information on the knowledge, skills and experience of the members of the Board are included in the “Report on corporate governance and ownership structure for the 2018 financial year”, prepared pursuant to art.123-bis TUF/CFA and published on the company website, in paragraph 4.2 “Composition”, which summarises the personal and professional characteristics of each director in office at the closing date of the financial year.

Bearing in mind that the self-assessment process showed a positive judgment on the commitment of each director and that the number of additional roles taken on by them does not affect the time they dedicate to carrying out the activities as directors of Banca IFIS or the commitment required in line with the role carried out within the board, please refer to the table included in the aforementioned “Report on corporate governance and ownership structure for the 2018 financial year” for the number of director positions assigned to board members.

In accordance with the provisions of Circular 285/2013 and the Corporate Governance Code, the Board of Directors set up its own Control and Risks Committee composed of four of the nine members of the Board of Directors chosen from among the non-executive directors, who are all independent.

During 2018 the Committee met 26 times, eight of which were jointly with the Board of Statutory Auditors and once jointly with the control body and the Supervisory Body. Since the beginning of 2019 until the date of approval of this document, the Committee held 6 meetings, of which 2 were held jointly with the Board of Statutory Auditors. The Control and Risks Committee supports the Board of Directors with regard to risk management and the internal control system, paying particular attention to the activities necessary for the Board to correctly and efficiently determine the Risk Appetite Framework and the risk management policies.

The information flow on risks for the Board of Directors, bases on the prior favourable approval of the Control and Risks Committee, is identified by means of a specific internal regulation and is mainly composed of documents prepared by the control functions and regarding the planning of activities and the related reporting (annual reports and quarterly dashboards, subsequently submitted to the Bank of Italy) as well as other verifications required by the legislation in force (reports on relevant risks undertaken by the Group, disclosure on checks concerning governance and management of liquidity risk, report on important operating functions outsourced, RAF, ICAAP and ILAAP reports, Recovery Plan, etc.).

In its capacity as the Parent Company, Banca IFIS is responsible for ensuring, through management and coordination activities, the overall consistency of the Group structures, and for verifying compliance by the subsidiaries with the provisions set out for the implementation of instructions of general and specific natures, issued by the Bank of Italy, in the interest of Group stability, specifically in relation to the supervisory reporting and regulation of corporate governance. In compliance with this principle, Banca IFIS Board of Directors expresses its opinion on remuneration and on the appointment of members of the corporate bodies of the subsidiaries. Based on the principle of corporate simplification pursued by the Bank, and in consideration of the fact that these bodies are required to operate within the management and coordination of the Parent Company, the Boards of Directors identified for the subsidiaries have limited scope both in terms of time and mandate, and most of the persons present within the bodies are a direct expression of the management and business of Banca IFIS; in this way, the immediate integration into the business segments in which the Group is involved is ensured as well as compliance with management instructions for the coordination of the Parent Company.

## 2. SCOPE OF APPLICATION (ART. 436 CRR)

The disclosure requirements set out in this document apply to Banca IFIS S.p.A., Parent company of the Banca IFIS Banking Group, enrolled in the Register of Banking Groups

The area of consolidation for the purposes of the budget is defined on the basis of the international accounting standards (IAS/IFRS) and more in particular by the IFRS 10, while the article 19 of the CRR provides for the inclusion for the purposes of prudential strengthening of the Holding Company of the banking group that is not consolidated in net equity.

For prudential purposes, consolidation policies provided for by the Bank of Italy's Circular no. 285 of 17 December 2013 (and subsequent updates) – “Supervisory Provisions for Banks” were adopted. In particular, the line-by-line consolidation was adopted for the banking, financial and instrumental companies belonging to the banking group.

Below is the scope of consolidation for prudential purposes and for the financial statements at 31 December 2018:

*Table 1 – Main information about Group companies*

| Company name | Sector | Headquarters | Rapporto di partecipazione | | | Voting rights |
|---|---|---|---|---|---|---|
| | | | Type of relationship (*) | Controlling company | % of share | |
| **La Scogliera S.p.A.** | Operating financial holding company | Mestre (Italy) | X | X | X | X |
| **Banca IFIS S.p.A.** | Banking activity | Mestre (Italy) | - | - | - | - |
| **IFIS FINANCE Sp. z o.o.** | Financial company | Warsaw (Poland) | 1 | BANCA IFIS S.p.A. | 100% | 100% |
| **IFIS Rental Services S.r.l.** | Non-financial company | Milan (Italy) | 1 | BANCA IFIS S.p.A. | 100% | 100% |
| **IFIS NPL S.p.A.** | Financial company | Mestre (Italy) | 1 | BANCA IFIS S.p.A. | 100% | 100% |
| **Cap.Ital.Fin. S.p.A.** | Financial company | Naples | 1 | BANCA IFIS S.p.A. | 100% | 100% |
| **Credifarma S.p.A.** | Financial company | Rome | 1 | BANCA IFIS S.p.A. | 70% | 70% |
| **Two Solar Park 2008 S.r.l.** | Non-financial company | Milan (Italy) | 1 | BANCA IFIS S.p.A. | 100% | 100% |
| **IFIS ABCP Programme S.r.l.** | Securitisation vehicle | Conegliano (Italy) | 4 | Altra | 0% | 0% |
| **Indigo Lease S.r.l.** | Securitisation vehicle | Conegliano (Italy) | 4 | Altra | 0% | 0% |

(*) Type of relationship:

1= majority of voting rights in the Ordinary Shareholders’ Meeting

2 = dominant influence during the Ordinary Shareholders’ Meeting

3 = agreements with other shareholders

4 = other forms of control

5 = unitary management as per art. 26, paragraph 1, of Italian Legislative Decree 87/92

6 = unitary management as per art. 26, paragraph 2, of Italian Legislative Decree 87/92

7 = joint control

It should be noted that the consolidation scope, for prudential purposes and for the financial statements at 31 December 2018, has undergone some changes from the previous year, due to the following events:

- acquisition of control of Cap.Ital.Fin. S.p.A., which took place on 2 February 2018;
- merger by incorporation of IFIS Leasing S.p.A. into Banca IFIS, which took place in May 2018;
- separation of Banca IFIS's NPL Area from the subsidiary IFIS NPL S.p.A., which took place in June 2018;
- acquisition of control of Credifarma S.p.A., which took place on 2 July 2018.

Please note that there are no obstacles within the Group that might hinder the quick transfer of capital resources or funds.

The subsidiaries at 31 December 2018 are included in the prudential consolidation scope on the same date, except for IFIS Rental Services S.r.l. and Two Solar Park 2008 S.r.l.

## 3. OWN FUNDS (ARTICLES 437 AND 492 OF CRR)

### Qualitative information

The new harmonised regulations for banks and investment firms included in Regulation (EU) no. 575/2013 (Capital Requirements Regulation, the so-called CRR) and in Directive 2013/36/EU (Capital Requirements Directive, the so-called CRD IV) entered into force on 1 January 2014. This regulatory framework, which is the only discipline that seeks to harmonise the prudential regulations of the Member States of the European Union, was transposed into Italian law with Circular no. 285 “Prudential supervisory provisions for banks” and no. 286 “Instructions for preparing the prudential reports for banks and brokerage firms”.

The new regulatory framework introduced important innovations especially as regards the methods to calculate capital for regulatory purposes (so-called “Own Funds”). In order to increase the quality of Banks’ capital, ordinary shares issued by the company and common equity reserves were preferred, while stricter criteria were set up for the eligibility of other capital instruments, and the recognition of minority interests was limited.

Effective January 2018, the transition period (2018-2022) aims at mitigating capital impacts resulting from adoption of the new IFRS 9 accounting standard; for more detailed quantitative and qualitative information, please refer to § **Errore. L'origine riferimento non è stata trovata.** of this document.

With the same effective date, the transitional provisions ended, which were introduced by Regulation no. 575/2013 (CRR) and were aimed at progressively mitigating the deduction from CET1 of “Deferred tax assets that are based on future profitability and not derived from temporary differences” (art. 478 CRR) and the partial recognition of minority interests (art. 480 CRR).

The prudential consolidation scope is different from the scope of the Banking Group since the Holding company, La Scogliera S.p.A., is included in application of art. 19 of the CRR, with a consequent recognition of minority interests among the consolidated own funds; the prudential consolidation scope does not include the subsidiaries IFIS Rental Services S.r.l. and Two Solar Park 2008 S.r.l. (consolidated using the equity method in compliance with art. 18 of the CRR). In particular, the regulation regarding the recognition of minority interests requires that the capital necessary to meet the minimum regulatory requirement is the lower between the subsidiary’s capital (% minimum requirement by the RWA of the subsidiary) and the consolidated capital (% minimum requirement by the RWA of the consolidated capital). The surplus between the total Own Funds and the minimum requirement can be recognised for the Group’s own share, attributing the remainder to minority interests.

### Quantitative information

The disclosure on the Group’s own funds requirements was prepared on the basis of the formats required by the Implementing Regulation (EU) 1423/2013, in accordance with the provisions of Part Eight, Title II of Regulation (EU) 575/2013.

### *3.1 Main characteristics of the items constituting Own Funds*

Own Funds consist of Tier 1 – T1, which in turn is made up of Common Equity Tier 1 – CET1, Additional Tier 1 – AT1, and Tier 2 – T2.

Common Equity Tier 1 capital (CET1) includes mainly:

- fully paid instruments and premium reserve;
- other reserves including retained earnings;
- minority interests allowed in CET1,

net of items to be deducted:

- goodwill and other intangible assets;
- deferred tax assets that are based on future profitability and do not derive from temporary differences net of the related tax liabilities.

Additional Tier 1 capital (AT1) includes minority interests allowed in AT1.

Tier 2 capital (T2) includes:

- fully paid-up subordinated loans that can be recognised in Tier 2 capital;
- minority interests allowed in T2.

### *3.2 Composition of Own Funds at 31 December 2018*

Common Equity Tier 1 Capital (CET1) includes:

- 11,1 million Euros in fully paid-up capital instruments;
- 10,9 million Euros in share premium;
- own CET1 instruments held directly for 1,4 million Euros;
- 747,9 million Euros in other reserves, including retained earnings.
- other cumulated income statement items, negative for 7,4 million Euros;
- 367,9 million Euros in minority interests given recognition in CET1.

The items to be deducted from CET1 include:

- 58,9 million Euros in goodwill and other intangible assets;
- deferred tax assets that are based on future profitability and do not derive from temporary differences net of the related tax liabilities, amounting to 145,9 million Euros.

The transitional provisions impacting on CET1 (+/-) include:

- positive adjustments to provisions for expected credit losses, in accordance with, equal to 222 thousand Euros (+) (Regulation 2017/2395);
- positive filter on negative actuarial reserves (IAS 19), equal to 6 thousand Euros (-) (CRR – art. 473 para. 3 and 4, letter d);

Additional Tier 1 capital (AT1) includes minority interests of 56,2 million Euros.

Tier 2 capital (T2) includes:

- fully paid-up subordinated loans that can be recognised in Tier 2 capital for an amount of 202,0 million Euros;
- minority interests of 75,2 million Euros.

| *Table 2 - Quantification of Own Funds* | 31.12.2018 |
|---|---|
| A. Common Equity Tier 1 - CET1 prior to the application of prudential filters | 1,128,913 |
| B. Prudential filters of the CET1 ( +/-) | |
| C. CET1 gross of the elements to be deducted and the effects of the transitional arrangements (A+/-B) | 1,128,913 |
| D. Deductions from CET1 | 204,844 |
| E. Transitional Arrangements - Impact on CET1 (+/-), including minority interests subject to transitional arrangements | 216 |
| F. Total Common Equity Tier 1 (TIER1 - CET1) (C-D +/-E) | 924,285 |
| G. Additional Tier 1 capital (Additional Tier 1 - AT1) gross of the elements to be deducted and the effects of the transitional arrangements | 56,178 |
| H. Elements to be deducted from AT1 | |
| I. Transitional Arrangements - Impact on AT1 (+/-), including the instruments issued by subsidiaries and included in the AT1 due to transitional provisions | |
| L. Total additional Tier 1 capital (Additional TIER1 - AT1) (G-H+/-I) | 56,178 |
| M. Tier 2 capital (Tier2 - T2) gross of the elements to be deducted and the effects of the transitional arrangements | 277,248 |
| N. Elements to be deducted from T2 | |
| O. Transitional regime - Impact on T2 (+/-), including instruments issued by subsidiaries that are given recognition in T2 pursuant to transitional provisions | |
| P. Total Tier 2 capital (Tier2 - T2) (M-N +/-O) | 277,248 |
| Q. Total own funds (F + L + P) (T) | 1,257,711 |

| | |
|---|---|
| *Q. Total own funds (F + L + P) (T-1)* | *1,191,097* |

### *3.3 Balance sheet reconciliation methodology*

The information required by the methodology to reconcile the balance sheet provided for by Annex I of Commission Implementing Regulation (EU) no. 1423/2013 dated 20 December 2013 is provided below.

***Table 3 - Balance Sheet Reconciliation***

| ASSETS | Scope of consolidation for accounting purposes | Scope of consolidation for regulatory purposes | Relevant amounts used to calculate Own Funds | Ref. Table “Transitional own funds disclosure template” |
|---|---|---|---|---|
| | | | | |
| 100. Intangible assets, of which: | 23.277 | 58.906 | -58.906 | 8 |
| *Goodwill* | *1515* | *37.144* | *-37.144* | 8 |
| *Other intangible assets* | *21.762* | *21.762* | *-21.762* | 8 |
| 110. Tax assets | 395.084 | 430.722 | -145.938 | |
| *a) current* | *46.820* | *45.755* | *0* | |
| *b) deferred* | *348.264* | *384.967* | *-145.938* | 10 |

| LIABILITIES AND NET EQUITY | Scope of consolidation for accounting purposes | Scope of consolidation for regulatory purposes | Relevant amounts used to calculate Own Funds | Ref. Table “Transitional own funds disclosure template” |
|---|---|---|---|---|
| 10. Financial liabilities valued at amortised cost - Securities in circulation | 1.979.002 | 1.979.002 | 202.024 | 46 |
| 120. Valuation reserves, of which: | -14.606 | -7.376 | -7.412 | 3-9-26a |
| *- foreign exchange differences* | *-6.032* | *-3.047* | *-3.047* | 3 |
| *- impact on overall profitability fair value measurement* | *-8.692* | *-4.390* | *-4390* | 3-26a |
| *- post-employment benefits discounting* | *118* | *61* | *25* | 3-9 |
| 150. Reserves | 1.168.543 | 703.613 | 703.834 | 2-3 |
| 160. Share premiums | 102.116 | 10.894 | 10.894 | 1 |
| 170. Share capital | 53.811 | 11.085 | 11.085 | 1 |
| 180. Treasury shares (-) | -3.103 | -1437 | -1437 | 16 |
| 190. Minority interests | 5.476 | 724.885 | 499.301 | 5 -34 -48 |
| 220. Profit for the period | 146.763 | 64.104 | 44.266 | 5a |

| | | | | |
|---|---|---|---|---|
| TOTAL TRANSITIONAL OWN FUNDS | | | 1.257.711 | |

BANCA IFIS

### *3.4 Capital instruments' main features template*

The information required by the capital instruments' main features template provided for by Annex II of the Commission Implementing Regulation (EU) no. 1423/2013 dated 20 December 2013 is provided below.

The capital instruments reported are all of the CET1 type, the unique identification code is not available as the shares of La Scogliera S.p.A. have no ISIN, the amount recognised in the regulatory capital and the par value of the instrument do not consider the share premium.

| | ***Table 4 - Capital instruments' main features template*** | |
|---|---|---|
| | **Capital instruments' main features template** | |
| 1 | Issuer: | LA SCOGLIERA S.p.A. |
| 2 | Unique identification code | |
| 3 | Law applicable to the instrument | Entire instrument - Italian Law |
| | **Regulatory treatment** | |
| 4 | CRR transitional provisions | Common Equity Tier 1 |
| 5 | CRR post-transitional provisions | Common Equity Tier 1 |
| 6 | Admissible at the level of the individual entity /(sub-)consolidation/of the individual entity and (sub-)consolidation | Individual entity and consolidated level |
| 7 | Type of instrument | Ordinary shares |
| 8 | Amount recognised in the regulatory capital (millions of Euro) | 9.64812 |
| 9 | Par value of the instrument (millions of Euro) | 9.64812 |
| 9a | Issue price | 5 |
| 9b | Redemption price | N/A |
| 10 | Accounting classification | Equity |
| 11 | Original issue date | N/A |
| 12 | Non-redeemable or at maturity | N/A |
| 13 | Original maturity date | N/A |
| 14 | Early redemption at the issuer's discretion subject to prior approval of the supervisory authority | N/A |
| 15 | Date of optional early redemption, date of possible early redemption and redemption amount | N/A |
| 16 | Subsequent dates for early redemption, if applicable | N/A |
| | **Coupons and dividends** | |
| 17 | Fixed or variable dividends/coupons | N/A |
| 18 | Coupon rate and any related index | N/A |
| 19 | Presence of dividend stoppers | N/A |
| 20a | Fully discretionary, partially discretionary or mandatory (in terms of time) | N/A |
| 20b | Fully discretionary, partially discretionary or mandatory (in terms of amount) | N/A |
| 21 | Presence of step up measures or other incentive for redemption | N/A |
| 22 | Non-cumulative or cumulative | N/A |
| 23 | Convertible or non-convertible | N/A |
| 24 | If convertible, event(s) that determines/determine the conversion | N/A |
| 25 | If convertible, in whole or in part | N/A |
| 26 | If convertible, conversion rate | N/A |
| 27 | If convertible, compulsory or optional conversion | N/A |

| | *Table 4 - Capital instruments' main features template* | |
|---|---|---|
| | **Capital instruments' main features template** | |
| 28 | If convertible, specify the type of instrument in which the conversion is possible | N/A |
| 29 | If convertible, specify the issuer of the instrument in which it is converted | N/A |
| 30 | Write down mechanisms | N/A |
| 31 | In case of a write-down mechanism, event(s) that determines/determine it | N/A |
| 32 | In the event of write-down, total or partial write-down | N/A |
| 33 | In the event of write-down, permanent or temporary write-down | N/A |
| 34 | In case of temporary write-down, a description of the revaluation mechanism | N/A |
| 35 | Position in the hierarchy of subordination in the event of liquidation (specify the type of instrument ranking immediately above (senior)) | N/A |
| 36 | Non-compliant characteristics of the instruments that benefit from the transitional provisions | N/A |
| 37 | If so, specify the non-compliant characteristics | N/A |

### 3.5 Own funds disclosure template

General own funds disclosure template provided for by Annex V of the Commission Implementing Regulation (EU) no. 1423/2013 dated 20 December 2013 is provided below.

***Table 5 - Own funds disclosure template***

| | | Amount at the Disclosure date |
|---|---|---|
| | **Common Equity Tier 1 capital: instruments and reserves** | |
| 1 | Capital instruments and the related share premium accounts | 21,979 |
| | *of which: ordinary shares* | 21,979 |
| 2 | Retained earnings | 632,060 |
| 3 | Accumulated other comprehensive income (and other reserves) | 64,363 |
| 5 | Minority interests (amounts allowed in consolidated CET1) | 367,898 |
| 5a | Independently reviewed interim profits net of any foreseeable charge or dividend | 44,266 |
| **6** | **Common Equity Tier 1 (CET1) before regulatory adjustments** | **1,130,566** |
| | **Common Equity Tier 1 (CET1): regulatory adjustments** | |
| 7 | Additional value adjustments (negative amount) | |
| 8 | Intangible assets (net of related tax liabilities) (negative amount) | -58,906 |
| 9 | Empty Set in EU | |
| 10 | Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liabilities where the conditions in article 38 (3) are met) (negative amount) | -145,938 |
| 12 | Negative amounts resulting from the calculation of expected loss amounts | |
| 16 | Common Equity Tier 1 instruments held directly or indirectly by the entity (negative amount) | -1,437 |
| **28** | **Total regulatory adjustments to the Common Equity Tier 1 (CET1)** | **-206,281** |
| **29** | **Common Equity Tier 1 (CET1)** | **924,285** |
| | **Additional Tier 1 (AT1):** | |
| 34 | Eligible Tier 1 included in the consolidated additional Tier 1 (including minority interests not included in line 5) issued by subsidiaries and held by third parties | 56,178 |
| 35 | of which: instruments issued by subsidiaries subject to progressive derecognition | |
| **36** | **Additional Tier 1 (AT1) net of regulatory adjustments** | **56,178** |
| | **Additional Tier 1 (AT1): regulatory adjustments** | |
| **43** | **Total regulatory adjustments to Additional Tier 1 (AT1)** | |
| **44** | **Additional Tier 1 (AT1)** | **56,178** |
| **45** | **Tier 1 (T1= CET1 + AT1)** | **980,463** |
| | **Tier 2: instruments and provisions** | |
| 46 | Capital instruments and the related share premium accounts | 202,023 |
| 48 | Eligible own funds instruments included in consolidated Tier 2 (including minority interests and additional Tier 1 instruments not included in line 5 or line 34) issued by subsidiaries and held by third parties | 75,225 |
| **51** | **Tier 2: before regulatory adjustments** | **277,248** |

| | Tier 2 (T2): regulatory adjustments | |
|---|---|---|
| **57** | **Total regulatory adjustments to Tier 2 (T2)** | |
| **58** | **Tier 2 (T2)** | **277,248** |
| **59** | **Total capital[1] (TC= T1+T2)** | **1,257,711** |
| **60** | **Total risk-weighted assets** | **8,974,645** |

| | Ratios and capital buffers | |
|---|---|---|
| 61 | Common Equity Tier 1 (as a percentage of the total risk exposure amount)[1] | 10.30% |
| 62 | Tier 1 capital (as a percentage of the total risk exposure amount)[1] | 10.92% |
| 63 | Total capital (as a percentage of the total risk exposure amount)[1] | 14.01% |
| 64 | Requirement of the institution's specific capital buffer (requirement for the Common Equity Tier 1 in accordance with article 92 (1) (a), requirements of capital conservation buffer, countercyclical capital buffer, systemic risk capital buffer and systemic entities capital buffer (as a percentage of the risk exposure amount) | 572,134 |
| 65 | of which: requirement of capital conservation buffer | 168,275 |
| 68 | Common Equity Tier 1 capital available for buffers (as a percentage of the risk exposure amount) (L) | 3.92% |

| | Amounts below the deduction thresholds (before risk-weighting) | |
|---|---|---|
| 72 | Capital of financial sector entities held directly or indirectly, when the institution does not have a significant investment in those entities (amounts below the threshold of 10% and net of eligible short positions) | 9,769 |
| 73 | Capital of financial sector entities held directly or indirectly, when the institution has a significant investment in those entities (amounts below the threshold of 10% and net of eligible short positions) | 5,500 |
| 75 | Deferred tax assets arising from temporary differences (amount below the 10% threshold, net of the related tax liabilities where the conditions in Article 38, paragraph 3 are met) | 749 |

### *3.6 Evolution of Own Funds*

Below is the information related to the evolution of Own Funds from the beginning of the period (01/01/2018) to the end of the period (31/12/2018) and the changes that occurred during the period under review.

| ***Table 6 - Evolution of Own Funds*** | |
|---|---|
| | **01/01/2018 - 31/12/2018** |
| **Common Equity Tier 1** | |
| **Beginning of the period** | |
| **Instruments and reserves (A)** | |
| 1. Equity (B) | 0 |
| 2. Reserves and share premiums | 72,392 |
| 3. Accumulated other comprehensive income, of which: (C) (C) | -5,708 |
| 3.1. Revaluation reserves of net actuarial losses and exchange differences on goodwill | 129 |
| 3.2 CRR: reserves of cash flow hedges, foreign exchange differences, unrealised profits/losses; etc. | |
| 4. Profit for the period (net of minority interests, charitable sums and Group foreseeable dividends) (D) | -11,723 |
| 5. Eligible minority interests (E) | 16,538 |
| **Regulatory adjustments** | |
| 11. Capital instruments held directly or indirectly, of which: | |
| 12. Goodwill | -681 |
| 13. Other intangible assets | 1,125 |
| 14. CRR: deferred tax assets based on future profitability excluding those arising from temporary differences | 25,370 |
| 20. Other transitional adjustments, of which: | -32,973 |
| 20.1 Transitional adjustment associated with IAS 19 (I) | -45 |
| 20.2 CRR: regulatory adjustments relating to unrealized profits and losses (J) | 1,334 |
| 20.3 CRR: transitional adjustment related to deferred tax assets based on future profitability, excluding those arising from temporary differences | -34,262 |
| **End of the period** | |
| | |
| **Additional Tier 1** | |
| **Beginning of the period** | |
| **Instruments** | |
| 22. Recognisable instruments, including instruments issued by subsidiaries (L) | 17,767 |
| **Regulatory adjustments** | |
| **End of the period** | |
| | |
| **Tier 2 capital** | |
| **Beginning of the period** | |
| 25. Recognisable subordinated instruments and loans (M) | -15,493 |
| 29.2 CRR: Transitional adjustment relating to unrealized profits on AFS securities subject to additional national filter (R) | |
| **End of the period** | |
| **Total Own Funds at the end of the period** | |
| | |
| **OWN FUNDS AT 31/12/2017** | **1,191,097** |
| **CHANGES** | **66,614** |
| **TOTAL** | **1,257,711** |

| | |
|---|---|
| **OWN FUNDS AT 31/12/2018** | **1,257,711** |

The positive change in own funds of € 66.6 million compared to 31 December 2017 is mainly attributable to:

- the inclusion of the profit for the year ended 31 December 2018 attributable to the Group calculated for regulatory purposes, net of the estimated dividend, for a total of € 44.3 million;
- greater inclusion of minority interests (Article 84 CRR), for an amount of € 18.8 million;
- the deduction from CET1 of 100% "Deferred tax assets that are based on future profitability and do not derive from temporary differences", due to the end of the transitional regime (Article 478 CRR) for an amount of € 145.9 million compared to € 137.0 million (equal to 80% in transitional regime) deducted at 31 December 2017; in this regard it should be noted that this deduction will however be progressively absorbed by the future use of these deferred tax assets;
- the positive change in reserves for the remaining part, including the profits generated by the Companies not included in the scope of the Banking Group, for the portion pertaining to the Group itself.

# 4. CAPITAL REQUIREMENTS (ART. 438 CRR)

Through the "Supervisory provisions for banks" (*Circular no. 285/13*), the Supervisory Authority governs the self-assessment process on capital adequacy carried out by the banks (*ICAAP – Internal Capital Adequacy Assessment Process*). In particular, Pillar 2 governs the prudential control process, organizing it into two integrated phases.

With the first phase intermediaries are required to carry out an independent assessment of their capital adequacy, current and future, in relation to the risks to which they are exposed and their own strategic choices. The second phase (SREP – Supervisory Review and Evaluation Process), carried out by the Supervisory Board, requires a review of this self-assessment process and the provision of an overall judgement on the intermediaries.

The Bank of Italy, following the supervisory review and evaluation process (*SREP*) carried out at the end of 2017, requested Banca IFIS Group to keep the same capital requirements communicated for 2017 also for 2018 fiscal year at consolidated level. The requirements include 1.875% of capital conservation buffer, that is:

- CET 1 capital ratio of 7.2% and binding to the extent of 5.4%
- Tier 1 capital ratio of 9.0% and binding to the extent of 7.2%
- Total capital ratio of 11.3% and binding to the extent of 9.5%.

In compliance with the principle of proportionality, and in consideration of the consolidated asset, the Group is in the category of Class 2 intermediaries. By virtue of the above and in line with its operational characteristics, the Banca IFIS Group determines the overall internal capital by adopting simplified methods on the quantification of the requirement for the risks of Pillar I and II and subsequent aggregation of the same (building block approach). Internal capital adequacy means the internal capital referred to all the relevant risks assumed and which the intermediary considers necessary to cover the losses exceeding an expected given level, including the possible requirements of internal capital due to considerations of a strategic nature.

Below is a summary table showing the methodology used to measure internal capital given the individual quantifiable Pillar I and Pillar II risks.

*Table 7 – Methods used to measure internal capital*

| CATEGORY | RISK TYPE | METHODOLOGY |
|---|---|---|
| FIRST PILLAR RISKS | **Credit Risk** | Standardised Approach |
| | **Counterparty Risk** | Mark to Market Method |
| | **Market Risk** | Standardised Approach |
| | **Operational Risk** | Basic Indicator Approach (BIA) |
| SECOND PILLAR RISKS | **Concentration Risk** | GA – Granularity Adjustment approach (Annex B, Title III, Circ. 285/13)<br>ABI method to estimate the Geo-sector Concentration Risk |
| | **Interest Rate Risk** | Simplified Approach (Annex C, Title III, Circ. 285/13) |

With regard to unquantifiable risks, on the other hand, the Banca IFIS Group has implemented appropriate internal control and mitigation measures, in compliance with the guidelines provided for by Bank of Italy in the above-mentioned legislation. As part of the measurement activities, stress tests are also defined and performed in terms of simplified sensitivity analysis on the main risks taken.

In the context of a progressive adaptation to international standards for liquidity risk measuring and monitoring (Basel 3), the short term indicator, the Liquidity Coverage Ratio (LCR), and the structural indicator, the Net Stable Funding Ratio (NSFR), were measured.

The prospective level is determined on an annual basis – during preparation of the ICAAP report – with reference to the end of the current period, taking into account the foreseeable development of the scope of application, the risks of the Group and operations. Any further assessments of the overall internal capital are also performed during the period in relation to any new or extraordinary events.

In order to prospectively assess the level of internal capital adequacy, the Banca IFIS Group:

- uses the industrial Plan, adequately detailing it with respect to the need for assessment of the risks;
- identifies the parameters that affect the incidence of risk, also anticipating its future evolution also in view of the expected trends of the relevant market;
- defines the estimates of evolution of the risk factors consistent with their economic and strategic scenarios;
- verifies the forecasts on the basis of multi-annual planning;
- carries out an estimate of the evolution of the accounting items that constitute the identified capital base;
- also considers any needs of a strategic nature.

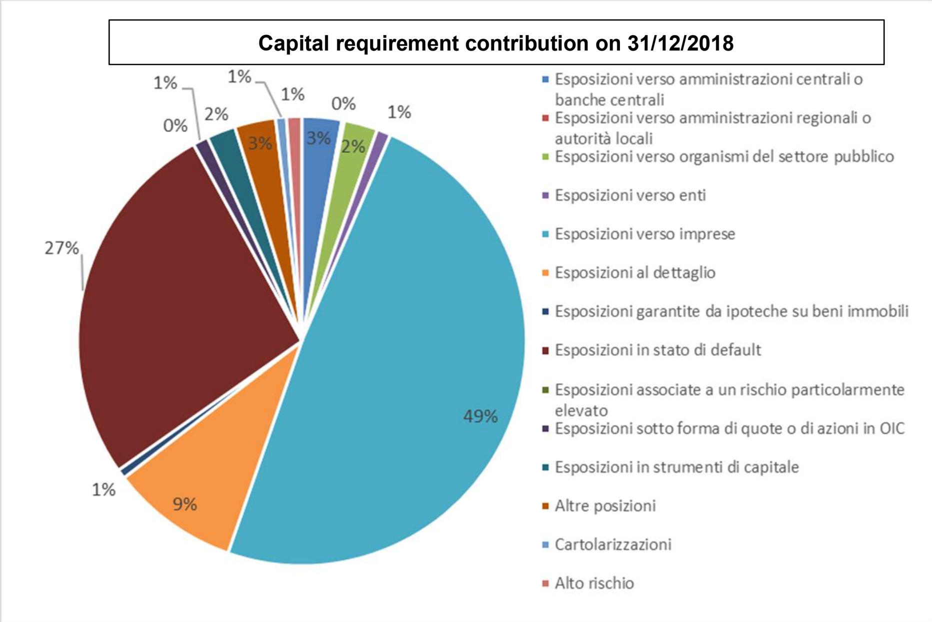
In order to cover the current and prospective internal capital adequacy, the Banca IFIS Group uses a definition of capital adequacy that coincides with that of regulatory Own Funds, prospectively assessed within the context of the Group's strategic plans.

Banca IFIS Group equity at 31 December 2018 is deemed adequate considering the overall exposure to risks.

***Table 8 - Credit and counterparty risk: capital requirement for each of the regulatory classes***

| ***Regulatory classes*** | **CREDIT RISK** | | **COUNTERPARTY RISK** | |
|---|---|---|---|---|
| *(in thousands of Euro)* | **Risk Weighted assets (RWA)** | **Capital requirement** | **Risk Weighted assets (RWA)** | **Capital requirement** |
| *Exposures to central governments or central banks* | 228,987 | 18,319 | | |
| *Exposures to regional governments or local authorities* | 14,922 | 1,194 | | |
| *Exposures to public sector bodies* | 193,048 | 15,444 | | |
| *Exposures to institutions* | 74,322 | 5,946 | 6,130 | 490 |
| *Exposures to corporations* | 3,900,328 | 312,026 | 11,698 | 936 |
| *Retail exposures* | 738,039 | 59,043 | | |
| *Exposures secured by mortgages on immovable property* | 53,823 | 4,306 | | |
| *Exposures in default* | 2,131,884 | 170,551 | 6,982 | 559 |
| *Exposures associated with particularly high risk* | | 0 | | |
| *Exposures in the form of units or shares in collective investment undertakings (UCIs)* | 87,527 | 7,002 | | |
| *Equity exposures* | 166,683 | 13,335 | | |
| *Other items* | 236,767 | 18,941 | | |
| *Securitisations* | 62,484 | 4,999 | | |
| *High risk* | 88,162 | 7,053 | | |
| **CAPITAL REQUIREMENT IN RELATION TO CREDIT AND COUNTERPARTY RISK** | **7,976,976** | **638,158** | **24,810** | **1,985** |

| | | | | |
|---|---|---|---|---|
| ***CAPITAL REQUIREMENT IN RELATION TO CREDIT AND COUNTERPARTY RISK (T-1)*** | ***6,492,339*** | ***519,387*** | ***8,874*** | ***710*** |




The internal capital in relation to market risk at 31/12/2018 amounted to 4.674 thousand Euros.

A brief overview of the measurements developed during the quantification of the internal capital absorbed by market risks follows:

| *Table 9 - Market risk: capital requirement for assets included in the trading book for supervisory purposes and for the entire financial statements* | | |
|---|---|---|
| | | |
| ***Risk type*** *(in thousands of Euro)* | **Risk-weighted asset (RWA)** | **Capital requirement** |
| *Position risk (Trading Book)* | 7,736 | 619 |
| *Settlement risk (Trading Book)* | | |
| *Commodities risk* | | |
| *Currency risk* | 50,691 | 4,055 |
| ***CAPITAL REQUIREMENT IN RELATION TO MARKET RISK*** | **58,427** | **4,674** |

| | | |
|---|---|---|
| ***CAPITAL REQUIREMENT IN RELATION TO MARKET RISK (T-1)*** | ***14,580*** | ***1,166*** |

The internal capital in relation to the credit valuation adjustment risk at 31/12/2018 amounted to 1.264 thousand Euro.

| *Table 10 - Capital requirement in relation to the credit valuation adjustment risk* | | |
|---|---|---|
| | | |
| ***Risk type*** *(in thousands of Euro)* | **Risk-weighted asset (RWA)** | **Capital requirement** |
| *CVA risk* | 15,802 | 1,264 |
| ***CAPITAL REQUIREMENT IN RELATION TO CVA RISK (T)*** | **15,802** | **1,264** |

| | | |
|---|---|---|
| ***CAPITAL REQUIREMENT IN RELATION TO CVA RISK (T-1)*** | ***21,590*** | ***1,727*** |

The internal capital in relation to operational risk at 31/12/2018 amounted to 71.890 thousand Euro.

| ***Table 11 - Capital requirement in relation to operational risk*** | |
|---|---|
| *(in thousands of Euro)* | |
| *Relevant Indicator December -2* | 452,598 |
| *Relevant Indicator December -1* | 560,643 |
| *Relevant Indicator December* | 424,565 |
| *Average relevant indicator of the last 3 years* | 479,269 |
| **CAPITAL REQUIREMENT IN RELATION TO OPERATIONAL RISK (T)** | **71,890** |
| ***CAPITAL REQUIREMENT IN RELATION TO OPERATIONAL RISK (T-1)*** | ***67,138*** |

The following table shows the capital ratios at 31 December 2018 in comparison with those at 31 December 2017.

| ***Table 12 - Capital ratios*** | ***31/12/2018*** | ***31/12/2017*** |
|---|---|---|
| *Common Equity Tier 1 (CET1)* | *924,285* | *859,944* |
| *Tier 1 capital* | *980,463* | *898,356* |
| *Total Equity Funds* | *1,257,711* | *1,191,097* |
| *Total RWA* | *8,974,645* | *7,376,606* |
| *Common Equity Tier 1 Ratio* | ***10.3%*** | ***11.7%*** |
| *CET1 minimum requirement* | *7.2%* | *6.6%* |
| *CET1 minimum requirement surplus* | *275,867* | *376,776* |
| *RWA surplus* | *2,678,619* | *3,231,990* |
| *Ratio - Tier 1 capital* | ***10.9%*** | ***12.2%*** |
| *T1 minimum requirement* | *9.0%* | *8.4%* |
| *T1 minimum requirement surplus* | *170,501* | *282,409* |
| *RWA surplus* | *1,560,680* | *2,318,928* |
| *Ratio - Total equity funds* | ***14.0%*** | ***16.2%*** |
| *Own Funds minimum requirement* | *11.3%* | *10.8%* |
| *Own Funds minimum requirement surplus* | *241,332* | *398,112* |
| *RWA surplus* | *1,722,075* | *2,465,554* |

It should also be noted that, on 28 January 2019, Bank of Italy requested the Banking Group to adopt for 2019 the following capital requirements at consolidated level, including 2.5% as a capital conservation reserve:

- CET 1 capital ratio of 8.12%, binding to the extent of 5.62%;
- Tier 1 capital ratio of 10.0%, binding to the extent of 7.5%;
- total capital ratio of 12.5%, binding to the extent of 10%.

As of 31 December 2018, the Banca IFIS Banking Group meets the aforementioned prudential requirements.

# 5. COUNTERPARTY RISK EXPOSURE (ART. 439 CRR)

## Qualitative disclosure

The counterparty risk is the risk that the counterparty to a transaction involving financial instruments defaults before the final settlement of the transaction cash flows.

The Banca IFIS Group does not carry out activities involving derivative financial products on behalf of third parties and has limited its operations to instruments from hedging against market risk. Banca IFIS sometimes uses financial derivatives designed to cover exposures on exchange rates.

At 31 December 2018, the Bank alone manages a residual portfolio of derivative products, mainly on interest rates, resulting from transactions concluded by the former subsidiary Interbanca with leading financial institutions and corporate customers included in the trading portfolio. On the same date, some derivative contracts on exchange rates related to the management of the Bank's foreign exchange position are also present in the same portfolio. As for the transactions being performed, it should be noted that the Group never undertakes actions of a speculative nature.

During 2018, no new derivative transactions on interest rates were carried out as this type of instrument was not included among the products offered to customers by the Bank.

With regard to counterparty risk connected to repos, its monitoring consists in a precise and constant verification of the structure and quality of the securities portfolio as the underlying risk is directly connected to the creditworthiness of the counterparties with which the collateralised financing operations are carried out (generally central counterparties such as Cassa di Compensazione e Garanzia and the European Central Bank) and is proportional to the price volatility of portfolio securities provided as a guarantee. There is only one repo transaction with central counterparty at the end of the fiscal year. In view of the regulatory provisions relating to SFT transactions executed with central counterparties (Cassa Compensazione e Garanzia and the European Central Bank) and accompanied by collateral on a daily basis, the impact in terms of capital requirement is zero.

For further information on the management processes followed by the Group, please refer to that shown in § 1.3.2 of this document.

## Quantitative disclosure

| ***Table 13 - Counterparty risk – mark to market method*** | | | |
|---|---|---|---|
| ***(units in thousands of Euro)*** | | | ***31/12/2018*** |
| ***Regulatory asset classes*** | ***Exposure value*** | ***Weighted value*** | ***Capital requirement*** |
| *Exposures to institutions* | *18,693* | *6,130* | *490* |
| *Exposures to companies and other subjects* | *11,697* | *11,698* | *936* |
| *Exposures in default* | *4,671* | *6,982* | *559* |
| ***Total*** | ***35,061*** | ***24,810*** | ***1,985*** |

*Table 14 – Financial derivatives*

*(in thousands of Euros)* **31 Dec 2018**

| *Type of underlying asset* | *Notional value* | *Positive gross fair value gross of compensation agreements* | *Positive fair value net of compensation agreements* | *Real guarantees received* | *Positive fair value net of compensation and guarantee agreements* | *Market value method Future exposure* | *Market value method EAD* |
|---|---|---|---|---|---|---|---|
| ***Trading portfolio for supervisory purposes*** | ***484,329*** | ***31,449*** | ***31,449*** | **-** | ***31,449*** | ***3,612*** | ***35,061*** |
| - Derivative contracts on debt securities and interest rates | 261,621 | 30,023 | 30,023 | - | 30,023 | 1,686 | 31,709 |
| - Derivative contracts on equity instruments and equity indices | 30,091 | - | - | - | - | - | - |
| - Derivative contracts on exchange rates and gold | 192,617 | 1,426 | 1,426 | - | 1,426 | 1,926 | 3,352 |
| - Derivative contracts on other values | - | - | - | - | - | - | - |
| ***Banking book – Hedging derivatives*** | **-** | **-** | **-** | **-** | **-** | **-** | **-** |
| - Derivative contracts on debt securities and interest rates | - | - | - | - | - | - | - |
| - Derivative contracts on equity instruments and equity indices | - | - | - | - | - | - | - |
| - Derivative contracts on exchange rates and gold | - | - | - | - | - | - | - |
| - Derivative contracts on other values | - | - | - | - | - | - | |
| ***Banking book - Other derivatives*** | **-** | **-** | | **-** | **-** | **-** | **-** |
| - Derivative contracts on debt securities and interest rates | - | - | - | **-** | - | **-** | **-** |
| #NOME? | - | - | - | - | - | - | - |
| - Derivative contracts on exchange rates and gold | - | - | - | - | - | - | - |
| - Derivative contracts on other values | - | - | - | - | - | - | - |
| ***Totale*** | ***484,329*** | ***31,449*** | ***31,449*** | **-** | ***31,449*** | ***3,612*** | ***35,061*** |

## 6. CAPITAL BUFFERS (ART. 440 CRR)

**Qualitative disclosure**

Starting from 1 January 2016, Banks must create a countercyclical capital buffer (CCyB) pursuant to art. 136 of Directive 2013/36/EU (CRD IV), in order to accumulate, during credit growth periods, Common Equity Tier 1 to be used in market stress situations.

Unlike the capital conservation buffer, the countercyclical capital buffer is only imposed during periods of credit growth and is calculated according to the provisions of the CRD IV by the competent national authorities.

**Quantitative disclosure**

As stipulated by article 140, paragraph 1 of EU directive 2013/36, the specific CCyB rate of the institution consists of the weighted average of the CCyB rates that are applied in the countries where the institution's significant credit exposures are located. The rate is subject to a quarterly review.

The European legislation was implemented in Italy with Bank of Italy Circular no. 285, which contains specific rules on CCyB. Based on the analysis of the reference indicators, the Bank of Italy has decided to maintain the CCyB rate (relative to exposures to Italian counterparties) at 0% for all of 2018. For other credit exposures, the Group uses the values of the CCyB rate established by the competent authorities of the counterparty State, in accordance with applicable regulations.

In this regard, the Banca IFIS Group, with reference to the date of 31 December 2018, in the absence of significant risk exposures to countries to which a specific non-zero CCyB rate is attributed, is not required to allocate provisions to this type of capital buffer.

The following is the information on the obligation to hold a countercyclical capital buffer pursuant to Article 440 of Regulation (EU) no. 575/2013, drafted according to the implementing technical standards contained in EU Regulation no. 2015/1555. The information shown below, referring to 31/12/2018, is at a consolidated level.

*Table 15 – Geographical breakdown of relevant credit exposures for the purpose of calculating the countercyclical capital buffer*

| Row | Breakdown by country | Generic credit exposures | | Exposure in the trading portfolio | | Exposure to securitisation | | Own funds requirements | | | | Weighting factors of own fund requirements | CCyB rate |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Value of the exposure by the SA method | Value of the exposure by the IRB method | Sum of the long and short position of the trading portfolio | Value of the exposure in the trading portfolio for internal templates | Value of the exposure by the SA method | Value of the exposure by the IRB method | Of which: generic credit exposures | Of which: exposures to securitization portfolios | Of which: exposure to securitization | Total | | |
| | | 010 | 020 | 030 | 040 | 050 | 060 | 070 | 080 | 090 | 100 | 110 | 120 |
| 010 | Italy | 9,348,361 | | 7,736 | | 62,473 | | 606,015 | 619 | 4,999 | **611,633** | 95.27% | 0.00% |
| | USA | 61,398 | | | | | | 4,912 | | | **4,912** | 0.77% | 0.00% |
| | Luxembourg | 57,341 | | | | | | 4,587 | | | **4,587** | 0.71% | 0.25% |
| | France | 43,292 | | | | | | 3,465 | | | **3,465** | 0.54% | 0.25% |
| | UK | 29,597 | | | | | | 2,378 | | | **2,378** | 0.37% | 1.00% |
| | Panama | 26,500 | | | | | | 2,120 | | | **2,120** | 0.33% | 0.00% |
| | Turkey | 23,437 | | | | | | 1,875 | | | **1,875** | 0.29% | 0.00% |
| | Switzerland | 21,172 | | | | | | 1,697 | | | **1,697** | 0.26% | 0.00% |
| | Netherlands | 17,342 | | | | | | 1,390 | | | **1,390** | 0.22% | 0.00% |
| | Gibraltar | 15,710 | | | | | | 1,257 | | | **1,257** | 0.20% | 0.00% |
| | Germany | 11,157 | | | | | | 971 | | | **971** | 0.15% | 0.00% |
| | People's Republic of China | 10,398 | | | | | | 832 | | | **832** | 0.13% | 0.00% |
| | Romania | 7,644 | | | | | | 624 | | | **624** | 0.10% | 0.00% |
| | Slovenia | 7,576 | | | | | | 606 | | | **606** | 0.09% | 0.00% |
| | Chile | 5,797 | | | | | | 464 | | | **464** | 0.07% | 0.00% |
| | Czech Republic | 5,013 | | | | | | 401 | | | **401** | 0.06% | 1.75% |
| | Sweden | 4,042 | | | | | | 323 | | | **323** | 0.05% | 2.50% |
| | Croatia | 4,029 | | | | | | 322 | | | **322** | 0.05% | 0.00% |
| | South Korea | 3,436 | | | | | | 275 | | | **275** | 0.04% | 0.00% |
| | Spain | 3,255 | | | | | | 267 | | | **267** | 0.04% | 0.00% |
| | Portugal | 2,716 | | | | | | 211 | | | **211** | 0.03% | 0.00% |
| | Mexico | 2,379 | | | | | | 190 | | | **190** | 0.03% | 0.00% |
| | Austria | 1,936 | | | | | | 155 | | | **155** | 0.02% | 0.00% |
| | India | 1,666 | | | | | | 133 | | | **133** | 0.02% | 0.00% |
| | Lithuania | 1,483 | | | | | | 119 | | | **119** | 0.02% | 1.00% |
| | Colombia | 1,423 | | | | | | 114 | | | **114** | 0.02% | 0.00% |
| | Slovak Republic | 1,211 | | | | | | 97 | | | **97** | 0.02% | 1.50% |
| | Belgium | 1,136 | | | | | | 97 | | | **97** | 0.02% | 0.00% |
| | Vietnam | 955 | | | | | | 76 | | | **76** | 0.01% | 0.00% |
| | Belarus | 922 | | | | | | 74 | | | **74** | 0.01% | 0.00% |
| | Poland | 837 | | | | | | 72 | | | **72** | 0.01% | 0.00% |
| | Malta | 555 | | | | | | 44 | | | **44** | 0.01% | 0.00% |
| | Saudi Arabia | 512 | | | | | | 41 | | | **41** | 0.01% | 0.00% |
| | Dubai | 475 | | | | | | 38 | | | **38** | 0.01% | 0.00% |
| | Japan | 451 | | | | | | 36 | | | **36** | 0.01% | 0.00% |
| | Hungary | 439 | | | | | | 35 | | | **35** | 0.01% | 0.00% |
| | Greece | 323 | | | | | | 26 | | | **26** | 0.00% | 0.00% |
| | San Marino | 299 | | | | | | 28 | | | **28** | 0.00% | 0.00% |
| | South Africa | 99 | | | | | | 8 | | | **8** | 0.00% | 0.00% |
| | Australia | 68 | | | | | | 5 | | | **5** | 0.00% | 0.00% |
| | Canada | 61 | | | | | | 6 | | | **6** | 0.00% | 0.00% |
| | Cyprus | 52 | | | | | | 4 | | | **4** | 0.00% | 0.00% |
| | Tunisia | 45 | | | | | | 4 | | | **4** | 0.00% | 0.00% |
| | Denmark | 38 | | | | | | 3 | | | **3** | 0.00% | 1.00% |
| | Norway | 34 | | | | | | 3 | | | **3** | 0.00% | 2.00% |
| | Albania | 33 | | | | | | 3 | | | **3** | 0.00% | 0.00% |
| | Ireland | 15 | | | | | | 1 | | | **1** | 0.00% | 1.00% |
| | Bulgaria | 10 | | | | | | 1 | | | **1** | 0.00% | 0.50% |
| | Brazil | 5 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Senegal | 4 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Argentina | 3 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Taiwan | 2 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Afghanistan | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Bolivia | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Egypt | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Ecuador | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Jamaica | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Guernsey | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Hong Kong | 1 | | | | | | 0 | | | **0** | 0.00% | 1.88% |
| | Israel | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Libya | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Morocco | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Nigeria | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Monaco | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Russia | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Serbia | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Syria | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Sudan | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Thailand | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| | Venezuela | 1 | | | | | | 0 | | | **0** | 0.00% | 0.00% |
| 020 | **Total Countries** | **9,726,702** | **-** | **7,736** | **-** | **62,473** | **-** | **636,408** | **619** | **4,999** | **642,026** | **100.00%** | |

***Table 16 - Amount of the institution's specific countercyclical capital buffer***

| *Row* | | *31/12/2018*<br>**Column**<br>*010* |
|---|---|---|
| *010* | Total amount of risk exposure | 9,796,911 |
| *020* | Institution's specific CCyB rate | 0.00% |
| *030* | Institution's specific countercyclical capital buffer requirement | - |

## 7. CREDIT RISK ADJUSTMENTS (Art. 442 CRR)

### Qualitative disclosure

***Definition of impaired loans used for accounting purposes.***

The definition of "impaired" loans adopted by the Banca IFIS Group for accounting purposes is the same as the one used for supervisory purposes. In particular, Circular no. 272 of 30 July 2008 as subsequently amended, "Matrix of accounts", within the context of the definition of parameters relating to credit quality, establishes:

*Financial assets are defined as "impaired" when they fall under the "Non-performing" category (...): bad loans, unlikely to pay and non-performing past due exposures and/or overdrafts.*

***Methodologies used to determine impairment losses***

At the end of every reporting period, including interim periods, receivables are reviewed in order to identify those objectively at risk of impairment following events occurred after their initial recognition. In accordance with the Bank of Italy's current regulations, this category includes loans which have been attributed the status of "non-performing", "unlikely to pay" or "past due", in compliance with the impairment rules of IFRS 9 as reported in detail in the disclosure of the Banca IFIS Group's 2018 Consolidated Financial Statements. Reversals on receivables are recorded against an improved quality of the exposure such as to lead to a decrease in the overall impairment previously recorded.

**Bad loans** are individually or collectively evaluated according to the cases listed below, and the total amount of the impairment loss on each loan is equal to the difference between the carrying amount at measurement (amortised cost) and the present value of expected future cash flows, calculated by applying the original effective interest rate. Expected cash flows are calculated taking into account expected recovery times, the estimated realisable value of any guarantees, as well as the expected costs to be incurred to recover the credit exposure. The original effective rate of each loan remains unchanged over time, even if there has been a restructuring of the relationship which led to a change in the contractual rate and even if the loan relationship becomes, in practice, non-interest bearing in terms of contractual interest. The original value of the loans is restored in subsequent years to the extent that the reasons that led to the adjustment no longer exist, provided that this assessment can be objectively linked to an event that occurred after the adjustment itself. Reversal on receivables is recorded in the income statement and cannot in any case exceed the amortised cost that the loan would have had in the absence of previous adjustments.

**Non-performing loans**, with the exception of those referable to retail portfolios of personal loans or mortgages, with a residual gross amount of less than 100 thousand euros, are subject to an individual assessment process. Non-performing loans with a gross residual amount of less than 100 thousand euros as well as non-performing loans with a gross residual amount greater than 100 thousand euros but whose classification dates back more than 10 years from the reference date are fully written down.

**Unlikely to pay loans**, with the exception of those referable to retail portfolios of personal loans or mortgages, with a residual gross amount greater than 100 thousand euros, are individually assessed, while those below the amount of 100 thousand euros are subject to a collective assessment of impairment.

The **acquired non-performing loans** pertaining to the NPL sector are the subject of a registration and evaluation process divided into the following phases:

- at the time of purchase, receivables are recognised by allocating the portfolio's purchase price among the individual receivables it consists of through the following steps:
    - accounting data of individual loans to a value equal to the contract price; this value is the one used for the reporting to the Central Credit Register;
    - after verifying the documentation, if provided in the contract, the Bank returns the loans lacking documentation or beyond the statute of limitations to the seller, and measures the fair value of receivables which actually exist and can be collected; finally, after sending a notice of assignment to the debtor, the Bank can start taking action to collect the receivable;
- once the collection process begins, receivables are measured at amortised cost using the effective interest rate method;
- the effective interest rate is calculated on the basis of the price paid, the transaction costs, if any, and the estimated cash flows and collection time calculated using either a proprietary model (point 5), or analytical estimates made by managers;
- the effective interest rate as set out in the previous point is unchanged over time;
- at the end of each reporting period, interest income accrued based on the original effective interest rate is recognised under Interest Income; these interests are calculated as follows: "Amortised Cost at the start of the period x IRR / 365 x days of the period";
- in addition, at the end of each reporting period, the expected cash flows for each position are re-estimated;
- should events occur (higher or lower revenues realised or expected compared to forecasts and/or a change in collection times) which cause a change in the amortised cost (calculated by discounting the new cash flows at the original effective rate compared to the amortised cost in the period), this change is also recognised under Interest Income;

For **other receivables**, a collective impairment assessment is carried out. Such measurement applies to categories of receivables with a homogeneous credit risk. The relevant losses are estimated as a percentage of the original loan amount by taking into account historical time series based on observable market data existing at the time of measurement and allowing to calculate the latent losses for each category.

## Quantitative disclosure

*Table 17 - Net credit exposure by type of exposure and counterparty (Art. 442 c)*

| *Portfolio/quality (thousands of Euros)* | Bad loans | Unlikely to pay | Impaired past due exposures | Not-impaired past due exposures | Not-impaired past due exposures | Total |
|---|---|---|---|---|---|---|
| *1. Financial assets at amortised cost* | 861.628 | 472.418 | 99.995 | 316.825 | 6.153.701 | **7.904.567** |
| *2. Financial assets at fair value through other comprehensive income* | - | - | - | - | 418.709 | **418.709** |
| *3. Financial assets designated at fair value* | - | - | - | - | - | **0** |
| *4. Other financial assets mandatorily measured at fair value* | - | 46953 | - | - | 6.277 | **53.230** |
| *5. Financial assets under disposal* | - | - | - | - | - | **0** |
| **Total** | **861.628** | **519.371** | **99.995** | **316.825** | **6.578.687** | **8.376.506** |

The table does not show the average values as it is believed that the period-end figure represents the risk exposure during the year.

| ***Table 18 - Geographical distribution of cash and "off-balance sheet" exposures to customers (art. 442 d)*** | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| ***Exposures/Geographical areas*** | **ITALY** | | **OTHER EUROPEAN COUNTRIES** | | **AMERICA** | | **ASIA** | | **REST OF THE WORLD** | |
| ***(thousands of Euros)*** | **Net exposure** | **Overall impairment losses/reversals** | **Net exposure** | **Overall impairment losses/reversals** | **Net exposure** | **Overall impairment losses/reversals** | **Net exposure** | **Overall impairment losses/reversals** | **Net exposure** | **Overall impairment losses/reversals** |
| **A. Cash exposures** | | | | | | | | | | |
| *A.1 Bad loans* | 861,676 | 181,662 | 208 | 88 | 11 | 0 | 5 | 0 | 6 | 0 |
| *A.2 Unlikely to pay* | 533,014 | 85,155 | 2561 | 2,086 | 7 | 0 | 0 | 0 | 4 | 0 |
| *A.3 Impaired past due exposures* | 95,713 | 9,058 | 2749 | 129 | 19 | 1 | 0 | 0 | 0 | 0 |
| *A.4 Not-impaired exposures* | 5,848,293 | 29,869 | 197343 | 1,891 | 97,532 | 1,002 | 16,288 | 129 | 166 | 1 |
| **Total A** | **7,338,696** | **305,744** | **202,861** | **4,194** | **97,569** | **1,003** | **16,293** | **129** | **176** | **1** |
| **B. Off-balance sheet exposures** | | | | | | | | | | |
| *B.1 Impaired exposures* | 122,876 | 1,887 | 1,746 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| *B.2 Not-impaired exposures* | 1,042,636 | 1,925 | 56,884 | 44 | 78 | 0 | 0 | 0 | 82 | 0 |
| **Total B** | **1,165,512** | **3,812** | **58,630** | **44** | **78** | **0** | **0** | **0** | **82** | **0** |
| **Total A+B** | **8,504,208** | **309,556** | **261,491** | **4,238** | **97,647** | **1,003** | **16,293** | **129** | **258** | **1** |

**Table 19 – Geographical distribution of cash and "off-balance sheet" exposures towards banks (art. 442d)**

| Exposures/Geographical areas | ITALY | | OTHER EUROPEAN COUNTRIES | | AMERICA | | ASIA | | REST OF THE WORLD | |
|---|---|---|---|---|---|---|---|---|---|---|
| (thousands of Euros) | Net exposure | Overall impairment losses/reversals | Net exposure | Overall impairment losses/reversals | Net exposure | Overall impairment losses/reversals | Net exposure | Overall impairment losses/reversals | Net exposure | Overall impairment losses/reversals |
| **A. Cash exposures** | | | | | | | | | | |
| *A.1 Bad loans* | | | | | | | | | | |
| *A.2 Unlikely to pay* | | | | | | | | | | |
| *A.3 Impaired past due exposures* | | | | | | | | | | |
| *A.4 Non impaired exposures* | 548,750 | 1,145 | 35,137 | 87 | 10,020 | 25 | | | | |
| **Total A** | 548,750 | 1,145 | 35,137 | 87 | 10,020 | 25 | **0** | **0** | **0** | **0** |
| **B. Off-balance sheet exposures** | | | | | | | | | | |
| *B.1 Bad loans* | | | | | | | | | | |
| *B.2 Unlikely to pay* | | | | | | | | | | |
| *B.3 Other impaired loans* | | | | | | | | | | |
| *B.4 Non impaired exposures* | 3,884 | - | 643 | - | **11261** | - | | | | |
| **Total B** | **3,884** | 0 | **643** | 0 | **11261** | **0** | **0** | **0** | **0** | **0** |
| **Total A+B** | **552,634** | **1,145** | **35,780** | **87** | **21,281** | **25** | **0** | **0** | **0** | **0** |

*Table 20 - Sector distribution of cash and "off-balance sheet" exposures towards customers (art. 442 e)*

| *Exposures/Counterparties (thousands of Euros)* | Public Administrations | | Financial institutions | | Financial institutions (of which: insurance companies) | | Non-financial institutions | | Families | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Net exposure | Overall impairment losses/reversals | Net exposure | Overall impairment losses/reversals | Net exposure | Overall impairment losses/reversals | Net exposure | Overall impairment losses/reversals | Net exposure | Overall impairment losses/reversals |
| **A. Cash exposures** | | | | | | | | | | |
| A.1 Bad loans | 1,431 | 4,294 | 2,376 | 8,478 | - | - | 167,426 | 154,264 | 690,673 | 14,714 |
| - of which forbearance exposures | - | - | 540 | 5,732 | - | - | 4,110 | 4,522 | 76,804 | 9 |
| A.2 Unlikely to pay | 2,614 | 395 | 38,358 | 1,093 | - | - | 186,141 | 77,819 | 308,473 | 7,934 |
| - of which forbearance exposures | 1,666 | 322 | 37,306 | 4 | - | - | 50,476 | 2,794 | 59,464 | 1,570 |
| A.3 Impaired past due exposures | 47,619 | 2,934 | 108 | 75 | - | - | 40,027 | 4,221 | 10,727 | 1,958 |
| - of which forbearance exposures | 44 | 1 | 18 | 8 | - | - | 1,145 | 79 | 708 | 285 |
| A.4 Non impaired exposures | 1,115,676 | 1,643 | 336,865 | 1,979 | - | - | 4,144,060 | 23,762 | 563,021 | 5,508 |
| - of which forbearance exposures | 51 | - | 3,839 | - | - | - | 16,597 | 191 | 9,205 | 526 |
| **Total A** | **1,167,340** | **9,266** | **377,707** | **11,625** | **-** | **-** | **4,537,654** | **260,066** | **1,572,894** | **30,114** |
| **B. "Off-balance sheet" exposures** | | | | | | | | | | |
| B.1 Impaired exposures | - | - | - | - | - | - | 108,476 | 1,877 | 16,146 | 10 |
| B.2 Not-impaired exposures | 695 | 440 | 144,533 | 703 | - | - | 670,918 | 767 | 283,534 | 59 |
| **Total B** | **695** | **440** | **144,533** | **703** | **-** | **-** | **779,394** | **2,644** | **299,680** | **69** |
| **Total (A+B)** | **1,168,035** | **9,706** | **522,240** | **12,328** | **-** | **-** | **5,317,048** | **262,710** | **1,872,574** | **30,183** |

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Table 21 shows the breakdown over time by residual contract duration of on and off-balance sheet transactions.

***Table 21 - Breakdown over time by the residual contract duration of financial assets (Art 442 f)***

| ***Items/Time periods*** *(thousands of Euros)* | **On demand** | **From 1 to 7 days** | **From 7 to 15 days** | **From 15 days to 1 month** | **From 1 to 3 months** | **From 3 to 6 months** | **From 6 months to 1 year** | **From 1 to 5 years** | **Over 5 years** | **Undetermined** | **Total** |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **On balance sheet assets** | | | | | | | | | | | |
| *Government securities* | 0 | 0 | 0 | 0 | 0 | 30,692 | 677 | 281,000 | 112,000 | 0 | **424,369** |
| *Other debt securities* | 173 | 0 | 0 | 707 | 262 | 1022 | 1,541 | 80867 | 99,176 | 0 | **183,748** |
| *UCITS units* | 99,350 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **99,350** |
| *Loans* | 1,357,522 | 72,497 | 218,359 | 495,691 | 1,361,840 | 535,474 | 601,715 | 2,139,154 | 628,427 | 327,913 | **7,738,592** |
| *- to banks* | 103,439 | 6,988 | 0 | 0 | 20,917 | 790 | 2222 | 8,024 | 3 | 280,960 | **423,343** |
| *- to customers* | 1,254,083 | 65,509 | 218,359 | 495,691 | 1,340,923 | 534,684 | 599,493 | 2,131,130 | 628,424 | 46,953 | **7,315,249** |
| **Off-balance sheet transactions** | | | | | | | | | | | |
| *Financial derivatives with exchange of underlying assets* | | | | | | | | | | | |
| *- long positions* | 0 | 0 | 17,700 | 60,000 | 115,200 | 0 | 0 | 0 | 0 | 0 | **192,900** |
| *- short positions* | 0 | 0 | 17,798 | 59,972 | 114,848 | 0 | 0 | 0 | 0 | 0 | **192,618** |
| *Financial derivatives without exchange of underlying assets* | | | | | | | | | | | |
| *- long positions* | 30,023 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **30,023** |
| *- short positions* | 30,970 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **30,970** |
| *Deposits and loans to be received* | | | | | | | | | | | |
| *- long positions* | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **0** |
| *- short positions* | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **0** |
| *Irrevocable commitments to grant funds* | | | | | | | | | | | |
| *- long positions* | 26,520 | 0 | 0 | 4471 | 37 | 1,980 | 1,177 | 36,776 | 88,654 | 0 | **159,615** |

| | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| *- short positions* | 74,992 | 0 | 0 | 3,033 | 0 | 1574 | 0 | 13319 | 66697 | 0 | **159,615** |
| *Financial guarantees granted* | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **0** |

With regard to the description of the process of determination of the impairment losses or reversals, reference should be made to the qualitative section of this document.

**Table 22 - On balance sheet exposures to customers: total value adjustment trend (Art. 442 i)**

| Reasons/categories (in thousands of Euros) | Bad loans | Unlikely to pay | Past due loans | Total |
|---|---|---|---|---|
| **A. Total initial adjustments** | **730,386** | **179,727** | **11,290** | **921,403** |
| *Effects of IFRS 9 adoption* | -293,123 | -98,961 | -1,555 | **-393,639** |
| **B. Increases** | **99,140** | **90,735** | **3,486** | **193,361** |
| *B.1 value adjustments from acquired or originated impaired financial assets* | - | 117 | - | **117** |
| *B.2. other value adjustments* | 74,530 | 72,020 | 1,398 | **147,948** |
| *B.3 losses on disposal* | - | - | - | **0** |
| *B.4 transfers from other categories of impaired exposures* | 23,808 | 637 | 5 | **24,450** |
| *B.5 contract changes without cancellations* | - | - | - | **0** |
| *B.6 other increases* | 802 | 17,961 | 2,083 | **20,846** |
| **C. Decreases** | **354,653** | **84,260** | **4,033** | **442,946** |
| *C.1 Impairment reversals from measurement* | 4 | 48 | 2 | **54** |
| *C.2 Impairment reversals from collection* | 7,483 | 41,054 | 2,249 | **50,786** |
| *C.3 gains on disposal* | - | - | - | **0** |
| *C.4 write-off* | 325,632 | 15,206 | - | **340,838** |
| *C.5 transfers to other categories of impaired exposures* | 50 | 23,800 | 600 | **24,450** |
| *C.6 contract changes without cancellations* | - | - | - | **0** |
| *C.7 other reductions* | 21,484 | 4,152 | 1,182 | **26,818** |
| **D. Total final adjustments** | **181,750** | **87,241** | **9,188** | **278,179** |

# 8. UNENCUMBERED ASSETS (ART. 443 CRR)

**Qualitative disclosure**

This chapter, in accordance with Article 443 of the (EU) regulation no. 575/2013 (CRR), includes unencumbered assets well as foreclosed assets.

Encumbered asset means every asset that has been pledged or that is the subject of an agreement to provide guarantees (securities or collaterals) or credit support to on- or off-balance sheet operations from which the asset cannot be freely withdrawn.

The pledged assets whose withdrawal is subject to any type of restriction, such as a prior approval before being withdrawn or replaced by other assets, are deemed to be encumbered.

The operations for which the Group normally binds part of its financial assets fall within the following categories:

- deposit with the Bank of Italy as a minimum reserve;
- transactions in derivative contracts;
- term deposits given as a guarantee to banks in syndicated transactions (*iblor deposit*);
- debt securities given as a guarantee to the Bank of Italy related to intraday advances;
- debt securities given as a guarantee to the European Central Bank for *TLTRO* operations;
- eligible receivables for collateralisation with the Bank of Italy through the *ABACO* program;
- assets used for securitisation transactions.

For further information on the management processes carried out by the Group, please refer to that shown in § 1.3.3 of this document.

**Quantitative disclosure**

The disclosure relating to the encumbered and unencumbered assets of the Group was prepared on the basis of the EBA/GL/2014/03 guidelines and the format required by the Implementing Regulation (EU) 2015/79, in accordance with the provisions of Part Eight, Title II of Regulation (EU) 575/2013.

The table below shows the amount of the encumbered and unencumbered assets by type of activity at 31 December 2018.

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| *Table 23 - Quantitative information on unencumbered assets (Euro/000) (ART. 443 and EBA/GL/2014/03 )* | | | | |
|---|---|---|---|---|
| ***ASSETS*** | ***Carrying amount of encumbered assets*** | ***Fair value of encumbered assets*** | ***Carrying amount of unencumbered assets*** | ***Fair value of unencumbered assets*** |
| ***Assets of the reporting institution*** | ***1,119,738*** | | ***8,290,254*** | |
| *Loans on demand* | | | *281,001* | |
| *Equity instruments* | | | *96,015* | *96,015* |
| *Debt securities* | *350,459* | *350,459* | *241,843* | *241,872* |
| *- of which: issued by general governments* | *350,459* | *350,459* | *60,869* | *60,869* |
| *- of which: issued by financial intermediaries* | | | *169,401* | *169,434* |
| *Loans other than on demand* | *769,279* | *109777* | *6,623,320* | |
| *Other assets* | | | *1,048,074* | |

| *Table 24 - Quantitative information on unencumbered assets (Euro/000) (ART. 443 and EBA/GL/2014/03)* | | |
|---|---|---|
| ***ENCUMBERED ASSETS AND ASSOCIATED LIABILITIES*** | ***Financial liabilities, contingent liabilities and securities lending*** | ***Assets, guarantees received and its issued debt securities foreclosed other than bank bonds guaranteed and ABS*** |
| ***Carrying amount of financial liabilities*** | ***1,600,490*** | ***1,140,625*** |
| *Deposits* | | |
| *Repurchase agreements* | | |
| *of which: with central banks* | | |
| *Collateralised deposits other than repos* | *1,600,490* | *1,140,625* |
| *of which: with central banks* | *695,972* | *502,846* |
| *Other* | | |

# 9. USE OF ECAIs (ART. 444 CRR)

## Qualitative disclosure

The Banca IFIS Group, for the purpose of calculating the capital requirement against credit and counterparty risk, avails itself of the services provided by external credit assessment institution (ECAI) "Fitch Ratings" for the positions included in the class "Exposures to central governments and central banks"; for the other asset classes, no external ratings are used.

The assessments of the ECAI selected apply to the following classes of activity:

***Table 25 – Portfolios and official ratings***

| *Regulatory classes* | ECA/ECAI | Rating features |
|---|---|---|
| *Exposures towards central governments and central banks* | *Fitch Ratings* | *Solicited/Unsolicited* |
| *Exposures to regional governments or local authorities* | | |
| *Exposures to public sector bodies* | | |
| *Exposures to institutions* | | |
| *Exposures to corporations* | | |
| *Retail exposures* | | |
| *Exposures in default* | | |
| *Exposures associated with particularly high risk* | | |
| *Equity exposures* | | |

The following table shows the mapping published by the Bank of Italy of long-term ratings issued by "Fitch Ratings".

| Classes of creditworthiness | Risk weighting coefficients | | | | ECAI |
|---|---|---|---|---|---|
| | Central governments and central banks | Supervised intermediaries, public sector agencies, territorial agencies | Multilateral development banks | Companies and other bodies | Fitch Ratings |
| 1 | 0% | 20% | 20% | 20% | from AAA to AA- |
| 2 | 20% | 50% | 50% | 50% | from A+ to A- |
| 3 | 50% | 100% | 50% | 100% | from BBB+ to BBB- |
| 4 | 100% | 100% | 100% | 100% | from BB+ to BB- |
| 5 | 100% | 100% | 100% | 150% | from B+ to B- |
| 6 | 150% | 150% | 150% | 150% | CCC+ and lower |

* In accordance with that established by the "New prudential supervisory provisions for banks", for these categories you must refer to the creditworthiness class in which the exposures to Central government is classified in which these bodies have their headquarters.

## Quantitative disclosure

The following table shows the breakdown of exposures subject to credit risk on the basis of weighting factors (classes of creditworthiness).

*Table 26 – Exposures by asset regulatory class and by class of creditworthiness/weighting (in thousands of Euro)*

| Asset regulatory class/weighting | 0% | 20% | 35% | 50% | 75% | 100% | 150% | 200% | 250 |
|---|---|---|---|---|---|---|---|---|---|
| *Exposures to central governments or central banks* | 1.050.287 | | | | | 227.110 | | | 75 |
| *Exposures to institutions* | 3.525 | 307.289 | | | | 5.244 | | | 5.50 |
| *Exposures to regional governments or local authorities* | | 74.612 | | | | | | | |
| *Exposures to public sector bodies* | | 419.941 | | | | 109.060 | | | |
| *Multilateral development banks* | | | | | | | | | |
| *International organisations* | | | | | | | | | |
| *Corporates and other entities* | | | | | | 3.940.089 | | | |
| *Retail exposures* | | | | | 1.177.969 | | | | |
| *Short-term exposures to corporates* | | | | | | | | | |
| *Exposures to CIUs* | | | | | | 87.527 | | | |
| *Exposures secured by mortgages on immovable property* | | | 80.515 | | 51.286 | | | | |
| *Exposures in default* | | | | | | 387.376 | 1.167.661 | | |
| *Exposures associated with particularly high risk* | | | | | | | 58.775 | | |
| *Securitisations* | | | | | | 62.452 | 21 | | |
| *Equity exposures* | | | | | | 166.683 | | | |
| *Other items* | 6.913 | 104 | | | | 236.746 | | | |
| **Total credit risk** | **1.060.725** | **801.946** | **80.515** | **51.286** | **1.177.969** | **5.222.287** | **1226.457** | **0** | **6.25** |

## 10. MARKET RISK EXPOSURE (ART. 445 CRR)

### Quantitative information

Exposure to market risk - as reported in § 1.3.3 for regulatory purposes, is calculated using the “standardised method”.

The following table details the regulatory requirements measured on 31 December 2018 for the Banking Group. The overall exposure refers to positions included in the trading portfolio for supervisory purposes of the Bank; the Banking Group, in reference to the contained positions included in the trading portfolio for supervisory purposes, essentially measured the position risk.

The capital requirement for own funds required for exchange rate risk amounts to € 4,055 thousand as the Banking Group, at the reference date, recorded a "total net open position in exchange rates" which exceeded 2% of the total of "Own funds" for consolidated use.

***Table 9 - Market risk: capital requirement for assets included in the trading book for supervisory purposes and for the entire financial statements***

| ***Risk type*** *(in thousands of Euro)* | **Risk-weighted asset (RWA)** | **Capital requirement** |
|---|---|---|
| *Position risk (Trading Book)* | 7,736 | 619 |
| *Settlement risk (Trading Book)* | | |
| *Commodities risk* | | |
| *Currency risk* | 50,691 | 4,055 |
| ***CAPITAL REQUIREMENT IN RELATION TO MARKET RISK*** | **58,427** | **4,674** |

| | | |
|---|---|---|
| ***CAPITAL REQUIREMENT IN RELATION TO MARKET RISK (T-1)*** | ***14,580*** | ***1,166*** |

## 11. OPERATIONAL RISK (ART. 446 CRR)

**Qualitative disclosure**

With reference to the measurement of capital requirements for operational risk, and having considered its own characteristics in terms of operations and size, the Banking Group adopts the “basic approach”, governed by Regulation (EU) no. 575/2013 of 26 June 2013 - Part Three, Title III and by Circular 285/2013 for its application in Italy for the purpose of calculating the regulatory capital requirement. In particular, it calculates the mandatory minimum capital requirement for operational risks by using the Basic Indicator Approach (BIA). The method quantifies the capital absorption in the amount of 15% of the average of the last three financial years of the “relevant indicator” values, referred to in art. 316 of Regulation (EU) no. 575/2013 of 26 June 2013, which is representative of the company operating volumes.

For regulatory purposes, operational risk is measured through IT procedures dedicated to the periodic production of statistical reports and consolidated prudential supervision.

At management level, reference is made to the management processes described in § 1.3.4 of this document for the measurement of operational risk.

In compliance with legislative provisions and the best practices in the sector, the Banca IFIS Group has already defined the overall framework for the management of operational risks. This framework consists of a set of rules, procedures, human, technological and organisational resources and control activities aimed at identifying, measuring, monitoring, preventing or mitigating, as well as communicating to the appropriate hierarchical levels, the operational risks assumed or assumable in the various organisational units. Key processes to correctly manage operational risk are represented by Loss Data Collection – LDC and the Risk Self-Assessment – RSA. In addition, another fundamental item of the operational risk governance and management process is represented by the adequate training of resources. Indeed, the Banca IFIS Group is constantly committed to the professional training and growth of its human resources.

With regard to the **Internal Loss Data Collection** process in use, operating losses are classified according to the risk categories defined by the Supervisory regulations and listed below:

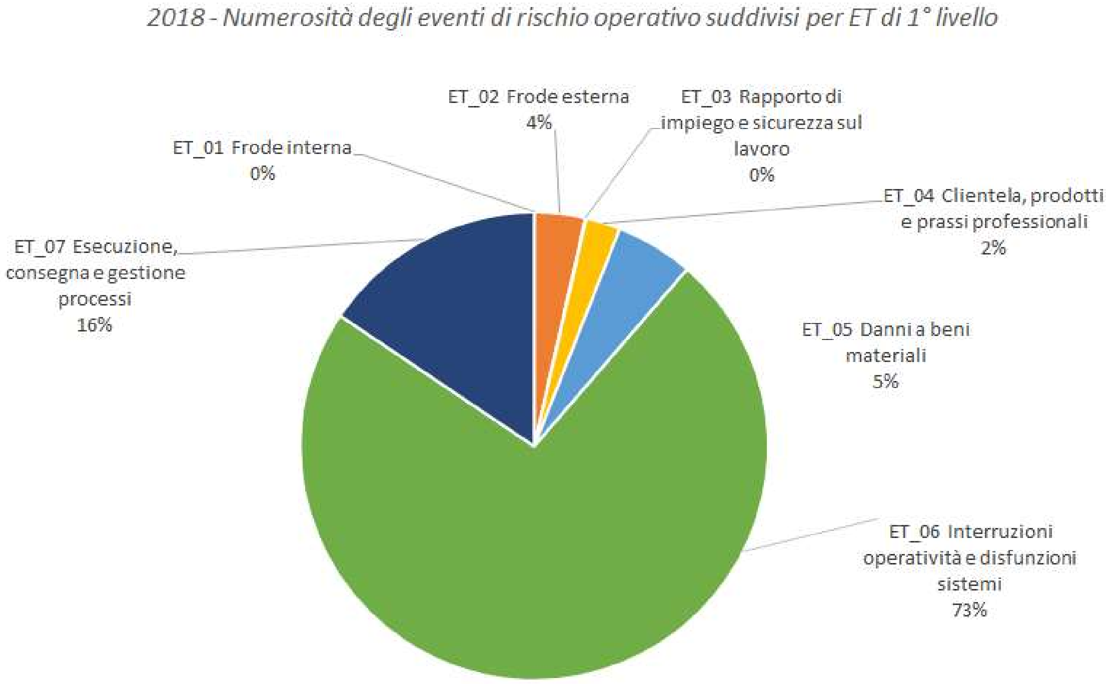
(a) internal fraud: losses due to unauthorised activity, fraud, embezzlement or violation of laws, regulations or company directives that involve at least one internal intermediary resource;
(b) external fraud: losses due to fraud, embezzlement, or violation of laws by subjects external to the intermediary;
(c) employment relationships and occupational safety: losses due to acts that are in non-compliance with the laws or agreements on employment, health and safety at work, the payment of compensation for personal injury or incidents of discrimination or diversity;
(d) customers, products and operating practices: losses resulting from non-fulfilment of professional obligations towards customers or from the nature or characteristics of the product or service provided;

(e) damage to tangible assets: losses resulting from external events, such as natural disasters, vandalism, terrorism, etc.;

(f) interruptions to operations and system malfunctions: losses due to interruptions to operations, malfunctions or unavailability of systems;

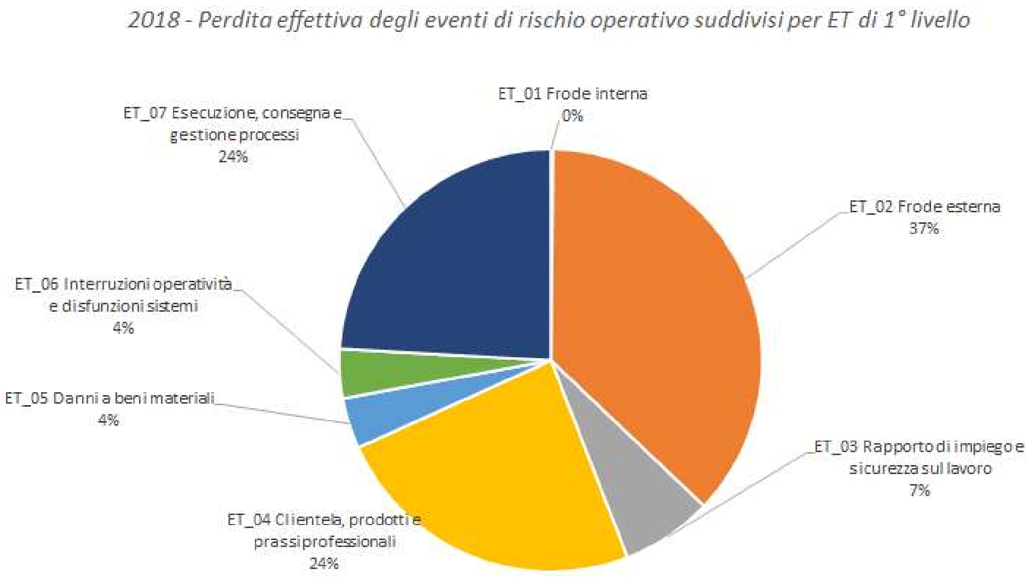
(g) execution, delivery and management of processes: losses due to shortcomings in the completion of transactions or in the management of processes, as well as losses due to relations with commercial counterparties, vendors, suppliers.

The results of the operational losses data collection of the Banking Group are shown in the graph below, which shows the percentage distribution of the number of registered events divided into the risk classes listed above:




| 2018 – Number of operational risk events subdivided by 1st level ET |
|---|
| ET-01 Internal fraud 0% |
| ET-02 External fraud 37% |
| ET-03 Employment relationship and occupational safety 7% |
| ET-04 Customers, products and operational practices 24% |
| ET-05 Damages to tangible assets 4% |
| ET-06 Operational interruptions and system malfunctions 4% |
| ET-07 Execution, delivery and management of processes 24% |

In the next chart, for completeness, the percentage distribution of the actual losses from registered operational risk events divided into 7 regulatory risk classes are shown.




| 2018 – Actual losses from operational risk event subdivided by 1st level ET |
|---|
| ET-01 Internal fraud 0% |
| ET-02 External fraud 37% |
| ET-03 Employment relationship and occupational safety 7% |
| ET-04 Customers, products and operational practices 24% |
| ET-05 Damages to tangible assets 4% |
| ET-06 Operational interruptions and system malfunctions 4% |
| ET-07 Execution, delivery and management of processes 24% |

For completeness, the ***Risk Control Self-Assessment*** process carried out in 2018 highlighted the potential risks to which the Banking Group is exposed on a prospective basis based on the self-assessments carried out by the main company process owners. Appropriate information on the identified areas for improvement and on the actions agreed for mitigation of potential risks is provided to the competent corporate bodies.

## Quantitative disclosure

The adoption of the “basic method” by the Bank resulted in a consolidated capital requirement on 31 December 2018 of approximately 72 million Euro, which was considered capable of coping with the unexpected financial impacts of potential risky events that could occur during 2019.

| ***Table 11 – Capital requirement in relation to operational risk*** | |
|---|---|
| *(in thousands of Euro)* | |
| *Relevant Indicator December -2* | 452,598 |
| *Relevant Indicator December -1* | 560,643 |
| *Relevant Indicator December* | 424,565 |
| *Average relevant indicator of the last 3 years* | 479,269 |
| **OPERATIONAL RISK CAPITAL REQUIREMENT (T)** | **71,890** |

| | |
|---|---|
| ***OPERATIONAL RISK CAPITAL REQUIREMENT (T-1)*** | ***67,138*** |

# 12. EXPOSURES IN EQUITY NOT INCLUDED IN THE TRADING PORTFOLIO (ART. 447 CRR)

## Qualitative information

As already reported in § 1.3.2 of this document in relation to participation risk, at 31 December 2018, the Group holds equity investment assets in its portfolio attributable to minority equity interests which are classified either among “Financial assets at fair value with impact on the overall profitability” or among “Financial assets mandatorily at fair value with impact on the income statement”.

In particular, the Group classifies among the “Financial assets at fair value with impact on overall profitability”, equity instruments not held for trading purposes, for which the option to designate at fair value is exercised at the time of initial recognition with impact on overall profitability (so called “OCI Option”). On the other hand, the equity instruments for which the Group does not apply this option are classified under “Financial assets mandatorily at fair value with impact on the income statement”.

***Recognition criteria***

*Financial assets at fair value through other comprehensive income*

The initial recognition of financial assets takes place on the settlement date. These assets are initially recognised at fair value inclusive of any transaction costs directly attributable to the instrument itself.

*Financial assets mandatorily measured at fair value through profit and loss*

The initial recognition of financial assets takes place on the settlement date. Upon initial recognition, financial assets held for trading are recognised at a value equal to the amount paid, understood as the fair value of the instrument, without considering the transaction costs or revenues directly attributable to the instrument, which are charged to the income statement.

***Measurement criteria***

*Financial assets at fair value through other comprehensive income*

The equity instruments for which the choice was made for classification in this category are measured at fair value and the amounts recognised as an offset of equity (Statement of comprehensive income) must not be subsequently transferred to the income statement, not even in the case of disposal. The only components referable to the equity instruments in question that are recorded in the income statement are the related dividends.

The fair value of financial instruments classified in this portfolio is based on prices recorded in active markets, on prices provided by market operators or on internal valuation models, generally used by financial practice, which take into account all risk factors related to the instruments and which are based on data that can be found on the market.

*Financial assets mandatorily measured at fair value through profit and loss*

Even after initial recognition, financial assets are measured at fair value and the effects of applying this criterion are recognized in the income statement. Fair value is determined on the basis of the criteria already illustrated for the financial assets measured at fair value with impact on overall profitability.

### Quantitative information

***Table 27 – Equity exposures – Banking book***

| *(in thousands of Euro)* | Carrying amount | | | Fair Value | | | Market Value | Profit/loss for the period | Capital gains/losses suspended in equity | Capital gains/losses suspended in equity and recognised among own funds |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Level 1** | **Level 2** | **Level 3** | **Level 1** | | | |
| **Equity instruments** | | | | | | | | | | |
| Financial assets mandatorily measured at fair value through profit and loss | | | 11,266 | | | 11,266 | | 11,266 | | |
| Financial assets at fair value through other comprehensive income | | | 13,385 | | | 13,385 | | | 1,712 | |
| | | | | | | | | | | |
| | | | | | | | | | | |
| **Total** | **-** | **-** | **24,651** | **-** | **-** | **24,651** | **-** | **11,266** | **1,712** | **-** |

## 13. EXPOSURE TO INTEREST RATE RISK ON POSITIONS NOT INCLUDED IN THE TRADING PORTFOLIO (ART. 448 CRR)

### Qualitative information

The assumption of interest rate risk is a normal part of banking and can be an important source of income and asset value. However, adverse movements in market interest rates can have negative effects on both the level of profits and the value of the capital of the Bank and its subsidiaries: changes in interest rates affect in fact the current income level through variations in interest margins and at the same time also affect the value of the assets, liabilities and off-balance sheet items. Therefore, an effective risk management system that maintains exposure to interest rate risk within acceptable levels is essential for the safety and financial soundness of the Group.

The interest rate risk on the banking portfolio is a transversal risk that affects all the Group companies and whose management is centralised at the Parent Company.

The assumption of significant interest rate risks is in principle unrelated to the management of the Group. The prevailing source of funding continues to consist of the “rendimax” online deposit account. Customer deposits on “rendimax” and “contomax” products are at a fixed rate for the term component, and at a non-indexed variable rate, which can be unilaterally reviewed by the Bank in compliance with the rules and contracts, for on-demand and on-call deposits.

During 2018 the strategy for diversifying funding sources continued; to that effect, the wholesale funding component was expanded by issuing a fixed-rate senior bond loan with a duration of 5 years for institutional investors within the “EMTN” program and by increasing the amount financed resulting from the securitisation at a variable rate with underlying factoring portfolio (three-year revolving program).

With regard to assets, customer loans remain mainly at variable rates, both with regard to the commercial credit component and to corporate loans.

Within the sphere of non-performing loan transactions (carried out by the subsidiary IFIS NPL), characterised by a business model focused on the purchase of receivables at lower values with respect to the nominal value, there is a potential interest rate risk connected to the uncertainty over collection times.

At 31 December 2018 the bond portfolio is composed (excluding the repurchases of notes from self-securitisation) mainly of government bonds indexed to the inflation rate. The average duration of this portfolio is around forty-five months.

For further information on the management processes followed by the Group, please refer to that shown in § 1.3.3 of this document.

**Quantitative information**

For the measurement of interest rate risk related to the “banking portfolio”, the Banking Group followed the simplified method prescribed by the Circular 285/2013 - Part One - Title III “Prudential Control Process” - Chapter 1 - Annex C , for the purposes of calculating the relevant regulatory capital requirement.

This methodology provides that all assets and liabilities are classified in time ranges based on their residual life, if a fixed rate applies, and on the repricing date if a floating rate applies. Within each time range, the net exposure, obtained from offsetting assets and liabilities, is calculated. The net exposures of each time range are then multiplied by the weighting factors obtained from the product, between the chosen hypothetical rate variation and the approximation of the modified duration related to each range.

The measurements developed during the quantification of the Internal Capital absorbed by the interest rate risk, as at 31 December 2018 is summarised in the table below.

***Table 28 - Interest rate risk on the banking book***

| | ASSETS | LIABILITIES | Net Exposure | Weighting Factor | Weighting Exposure |
|---|---|---|---|---|---|
| On demand | 425,302 | -269,802 | 155,500 | 0.00% | - |
| up to 1 month | 3,287,533 | -1,163,214 | 2,124,319 | 0.01% | 123 |
| from 1 to 3 months | 1,049,142 | -1,367,212 | -318,070 | 0.02% | - 62 |
| from 3 to 6 months | 779,095 | -300,586 | 478,509 | 0.04% | 196 |
| from 6 months to 1 year | 340,570 | -742,681 | -402,110 | 0.07% | - 297 |
| from 1 to 2 years | 332,360 | -1,360,834 | -1,028,473 | 0.20% | - 2.059 |
| from 2 to 3 years | 474,156 | -1,187,481 | -713,325 | 0.58% | - 4.125 |
| from 3 to 4 years | 547,474 | -655,491 | -108,016 | 1.11% | - 1.200 |
| from 4 to 5 years | 508,609 | -395,822 | 112,787 | 1.70% | 1,917 |
| from 5 to 7 years | 317,808 | 0 | 317,808 | 2.76% | 8,767 |
| from 7 to 10 years | 61,882 | 0 | 61,882 | 4.17% | 2,582 |
| from 10 to 15 years | 33,498 | 0 | 33,498 | 6.31% | 2,113 |
| from 15 years to 20 years | 4,298 | 0 | 4,298 | 8.48% | 365 |
| over 20 years | 1,701 | 0 | 1,701 | 10.71% | 182 |

| | |
|---|---|
| Change in company economic value | 8,502 |
| Own funds | 1,257,711 |
| Risk profile indicator (warning threshold 20%) | 0.68% |

# 14. EXPOSURE TO SECURITISATION POSITIONS (ART. 449 CRR)

## Qualitative information

This section provides an illustration of the Group's exposures to securitisation transactions; in these operations the Group plays the role of originator, sponsor or investor, depending on the case.

The Bank has adopted a "Policy for the management of securitisation transactions" with which it governs the process for managing securitisation transactions in the event that it intervenes in the role of "investor" (i.e. subscriber of securities) or of "sponsor" (i.e. that is, subject that structures the operation). The policy clearly defines, for each of the cases identified, the tasks of the organisational units and the corporate bodies involved, both with reference to the preparatory due diligence activities and with regard to the continuous monitoring of the performance of the transaction.

***IFIS ABCP Programme securitisation transaction***

On 7 October 2016, a three-year revolving securitisation program was launched for trade receivables from assigned debtors. Against the initial transfer of the loans by Banca IFIS (originator) for an amount of €1,254.3 million, the vehicle called IFIS ABCP Programme S.r.l. issued senior securities, subscribed by investment vehicles which refer to the co-arranger banks of the transaction, for an amount of € 850 million, increasing to € 1,000 million during the second quarter of 2018. An additional portion of senior securities, with a maximum nominal value of € 150 million, initially subscribed for € 19.2 million, with subsequent adjustment based on the composition of the backed up portfolio, was subscribed by Banca IFIS, which will use this security as collateral in refinancing operations with third parties. On 31 December 2018, the share subscribed by the Bank reached a maximum amount of € 150 million. The difference between the value of the receivables portfolio and the senior securities issued represents the credit support for the holders of the same securities, which takes the form of a deferred purchase price.

The servicing activity is carried out by Banca IFIS itself which, with its own structure, is responsible for:

- following daily the activities for managing collections and checking cash flows;
- ensuring at every cut-off *date* the balancing of data for every period end;
- proceeding at each cut-off date with the verification, completion and transmission of the Service report containing the information on the securitised portfolio required by the vehicle and the lending banks.

The securitisation program requires the collections received by the Bank to be transmitted to the vehicle on a daily basis, while the periodic transfers of the new portfolio take place about six times a month; in this way a close elapsed time is guaranteed between the outflows from the Bank and the incoming flows relating to the payment of the new assignments.

It should be noted that the receivables from securitised debtors are only partially recorded in the balance sheet assets, in particular the non-recourse loans that the Bank purchased from the transferor, or with the transfer to the transferee of all the risks and benefits. The tables shown in the quantitative information therefore only show this portion of the portfolio.

In compliance with the IAS / IFRS accounting principles, the securitisation transaction does not represent a substantial transfer of all the risks and benefits, as it does not meet the requirements for derecognition. Furthermore, the vehicles were consolidated in order to better represent the operation as a whole.

The maximum theoretical loss that Banca IFIS can suffer is represented by any losses that may occur within the reassigned receivables portfolio, whose impacts are the same as those that Banca IFIS would suffer in the absence of the securitisation program itself; consequently, securitisation in the financial statements was recorded as follows:

- non-recourse securitised receivables are recorded, as part of “receivables due from customers”, under the sub-item “factoring”;
- the financing obtained through the issue of senior securities subscribed by third parties was recorded under “outstanding securities”;
- interest income on receivables are recorded in the financial statements under the same item, “interest income on receivables due from customers”;
- interest expenses matured on securities are recorded under “interest expenses and similar charges” in the sub-item “outstanding securities”;
- the transaction organisation fees were fully expensed in the income statement for the year in which the program began.

On 31 December 2018, interest expenses on senior notes recorded in the income statement amounted to € 7.6 million.

***Third-party securitisation transactions***

On 31 December 2018, the Group holds a portfolio of securities as a result of third-party securitisations. Specifically, these consist of five separate third-party securitisation transactions having underlying respectively two non-performing secured loan portfolios, a speculative mortgage loan, a minibond portfolio issued by Italian listed companies and a non-performing loan portfolio partially secured by mortgages whose securitisation is assisted by a State guarantee.

The main features of the outstanding transactions at the reference date are shown below:

- “San Marco” securitisation: this consists of a securitisation of a non-performing secured mortgage loan portfolio with a total nominal value of approximately € 160 million and maturity in September 2022 in which the Parent Company participates as Senior Noteholder and Sponsor, subscribing all of the senior tranches as at 31 December 2018, equal to € 19.7 million, and 5% of junior tranches, for € 0.7 million, which were issued by the vehicle Tiberio SPV S.r.l;
- “Project Firenze” securitisation: this consists of a securitisation of a non-performing portfolio composed of secured bank positions mainly with SMEs with a total nominal value of approximately € 264 million and maturity in 2023. In this operation the notes were issued by the vehicle Orione SPE S.r.l. and the Parent Company participated as Senior

Noteholder and Sponsor, subscribing 100% of the senior tranches on 31 December 2018 for a value of € 34.8 million as well as 5% of the junior tranches for € 1.1 million;

- “Five V” securitisation: the transaction, started at the end of November 2017, consists of a securitisation through the vehicle Ballade SPV S.r.l. having only an underlying mortgage loan classified as non-performing, with a nominal value of € 20 million and a maturity in October 2020 in which the Parent Company participates, also in this case, as Senior Noteholder and Sponsor, becoming the holder of 100% of senior securities for € 2.1 million and 5% of junior securities; the transaction is substantially closed following the sale of the underlying asset to the mortgage credit;
- “Elite Basket Bond (EBB)” securitisation, for which the vehicle EBB S.r.l. issued at a price equal to the nominal value, for a total of € 122 million, of Asset Backed Securities (ABS) in a single tranche with a duration up to December 2027 and an underlying portfolio (“Basket”) of minibonds issued by 11 Italian listed companies. The peculiarity of this operation consists in the fact that these securities are senior unsecured bonds but they benefit from a mutual Credit Enhancement equal to 15% of the total amount of the transaction (€ 24 million), to be used in the event of delays and/or insolvencies on the part of the issuing companies for the payment of interest and/or capital on the minibonds. The Parent Company participates in this transaction solely as an underwriter, by registering a portion of the above tranche in its assets, equal to € 6.0 million;
- “FINO 1” securitisation: this consists of an investment as a Senior Noteholder in a securitisation transaction whose issued tranches are backed by the “GACS” State guarantee (Non-performing Securitisation Guarantee) and with underlying non-performing positions with an original total nominal value of approximately € 5.4 billion. The tranche to be subscribed for originally € 92.5 million by Banca IFIS (on a total nominal value of € 650 million) is the Class A Senior Note, characterised by maturity in October 2045. On 31 December 2018, the portion of the tranche subscribed, net of repayments during the year, has a statement value of € 77.6 million.

For the sake of completeness, it should be noted that the Group holds, through the broader intervention carried out in 2017 by the Voluntary Scheme of the Interbank Deposit Protection Fund, shares of mezzanine and junior notes of the “Berenice” securitisation for a total of € 0.1 million.

***Self-securitisation transactions***

During December 2016, the Banca IFIS Group, through the now merged company IFIS Leasing S.p.A. (originator), completed a securitisation transaction which involved the sale to the vehicle company Indigo Lease S.r.l. of a portfolio of performing loans for a total of € 489 million.

The transaction was assigned a rating by Moody's and by DBRS. The same agencies will look after the annual monitoring for the entire duration of the operation.

The spot price of the loan portfolio sold, amounting to € 489 million, was paid by the vehicle to the merged company IFIS Leasing S.p.A. using the funds arising from the issue of senior securities for the amount of € 366 million, which was assigned a rating of Aa3 (sf) (Moody's) and AA (sf) (DBRS), whose repayment is linked to collections made on the loan portfolio. In addition, junior securities purchased by the merged company IFIS Leasing S.p.A., for which a rating was not assigned, were issued by the vehicle for a value of € 138 million. Furthermore, the latter was given a specific servicing mandate for the collection and management of receivables.

During the third quarter of 2017, the parent company Banca IFIS S.p.A. repurchased all the senior securities issued by the vehicle. As at 31 December 2018, all the securities issued by the vehicle were therefore subscribed by the Banca IFIS Group.

Please note that, due to the contractual conditions underlying the transaction, there is no substantial transfer of all the risks and benefits relating to the assets sold (receivables).

**Quantitative information**

Please refer to the tables in section E of the Notes to the Consolidated Financial Statements of the Banca IFIS Group 2018.

# 15. REMUNERATION POLICY (ART. 450 CRR)

The main bodies and persons involved in setting up and approving the remuneration and incentive policies are: the Shareholders' Meeting, the Board of Directors; the Remuneration Committee; the CEO; the General Manager; the Control Functions; the Human Resources Department and the Strategic Planning and Management Control Department.

The role of these bodies, within said scope, is described in the Articles of Association and/or in the corporate regulations, as detailed below.

## 15.1 Process and persons involved

***Shareholders' Meeting***

In accordance with art. 10 of the Articles of Association, the Ordinary Shareholders' Meeting, *"in addition to establishing the remuneration of the bodies it has appointed, resolves on:*

- *the remuneration policies concerning the Board of Directors, the CEO, the Board of Statutory Auditors, the General Manager and the rest of the personnel;*
- *any remuneration plans based on financial instruments;*
- *the criteria to determine the remuneration to be paid in the case of an early termination of an employment relationship or early termination of an office, including the maximum limits set for this remuneration in terms of annual fixed amount and the maximum amount deriving from their application".*

The Shareholders' Meetings can also:

- establish the remuneration for the members of the Board of Directors, pursuant to art. 2389 of the Italian Civil Code;
- determine a total remuneration of all the Board members, including those holding special offices.

***Board of Directors***

The Board of Directors, according to the provisions of Article 14 of the Articles of Association, has exclusive jurisdiction over resolutions concerning *"nomination, revocation and financial remuneration of members of General Management"* and *"remuneration and incentive policies to be submitted to the Shareholders' Meeting, the review, at least annually, of these policies and the responsibility for their correct implementation, also with the task of ensuring that the remuneration policy is adequately documented and accessible within the corporate structure"*.

In addition, pursuant to Article 10 of the Articles of Association, the Board of Directors, with the favourable opinion of the Board of Statutory Auditors, may also determine the remuneration of Directors assigned special tasks.

During the preliminary phase, the Board avails itself of its own internal Committee, the Remuneration Committee, as specified below.

***Remuneration Committee***

The Remuneration Committee, set up within the Board of Directors of the Parent Company, performs support functions for the Board of Directors in defining the remuneration and incentive policies of the Group. More specifically, according to the provisions of the related Regulations, it is responsible for:

- *"providing consulting services and submitting proposals to the Parent Company's Board of Directors concerning the remuneration and incentives to be provided to company representatives (including executive directors and other directors with special offices), of executives with strategic responsibilities and of the heads of the internal control functions of the Parent Company and of the other Group subsidiaries, as well as the establishment of performance goals related to the variable component of the remuneration;*
- *providing advice to determine the criteria for the remuneration of the remaining "key" personnel identified within the Parent Company and the other Group companies in compliance with current supervisory regulations;*
- *directly overseeing the proper application of rules pertaining to the remuneration of the heads of the internal control functions of the Parent Company and of the other Group subsidiaries, working closely with the Board of Statutory Auditors;*
- *preparing the documents to be submitted to the Board of Directors of the Parent Company for the relevant decisions;*
- *collaborating with other internal committees of the Board of Directors, in particular with the Control and Risks Committee, where the coincidence of a significant component of members of both Committees does not guarantee ipso facto such cooperation;*
- *ensuring the involvement of the Internal Audit, Human Resources, Strategic Planning, Risk Management and of Compliance departments of the Parent Company in the process of preparing and monitoring remuneration policies and practices of the Group;*
- *monitoring the application of decisions adopted by the Board of Directors of the Parent Company and of the other Group subsidiaries as far as remuneration is concerned and, specifically, also based on the information provided by the company departments, providing an opinion on the achievement of performance objectives on which the incentive plans are based and on the verification of the other conditions established for the disbursement of remuneration;*
- *making proposals to the Board of Directors of the Parent Company with respect to the criteria for granting stock options or shares in favour of Group's directors and employees;*
- with regards to the latter, if possible, providing an interpretation in controversial cases and adjusting the granting conditions of each tranche as well as regulating the exercise of relevant rights in case of transactions of an extraordinary nature involving the Parent Company's capital (mergers, increases in free or paid capital, share splits and reverse share splits, etc.)".

Pursuant to said regulations, the Chairman of the Committee reports to the Board of Directors about the activities carried out at the first possible meeting. In addition, the Committee evaluates, at least on an annual basis, the adequacy of, overall compliance with and actual application of the remuneration policies of the Group and reports to the Shareholders' Meeting of the Parent Company about the activities carried out.

Composition

The Remuneration Committee is made up of three members chosen from among the non-executive members of the Parent Company's Board of Directors, the majority of whom are independent.

As approved by the Board of Directors at its meeting of 22 March 2016, the members of the Committee are: Francesca Maderna (non-executive and independent director), who is responsible for presiding over the Committee; Daniele Santosuosso (non-executive and independent director) and finally Riccardo Preve (non-executive and non-independent director).

Working method

The Committee's term of office lasts for three years. Its members meet periodically, including through video/telephone conference, any time the need arises in connection with the tasks assigned to them.

If one or more members of the Committee are no longer in office, the Board of Directors can arrange for the appointment and if necessary the replacement of these members. As established by current Regulations, the President of the Parent Company's Board of Statutory Auditors, or another standing Statutory Auditor delegated by them on a case-by-case basis, attends Committee meetings. The other members of the Board of Statutory Auditors may also participate and if there are not items in the agenda that do not directly concern them, the CEO and the General Manager of the Parent Company may participate as well. Furthermore, no Director may participate in the meetings of the Committee when the proposals for the remunerations of the Board's members are being discussed. The President of the Committee assesses, in relation to the matters to be discussed, the need to involve the Head of Risk Management to ensure that the incentive schemes are properly adjusted to take account of all the risks assumed by the Group, according to methods that are consistent with those adopted for risk management for regulatory and internal purposes. The Committee may request the presence:

- of external remuneration experts, which may also be identified among the Parent Company's members of the Board of Directors, provided that such experts do not provide significant services also to the Human Resources Department, to the executive directors or to the executives with strategic responsibilities of the Parent Company and/or other Group companies, which could actually compromise the independent opinion of the consultants themselves;
- any other representative or company staff of the Parent Company or of another Group company.

The Committee may access all company information deemed relevant to perform its tasks and may use, autonomously, the financial resources established by the Board and with reporting obligations with regards to any use of funds, at least once a year, usually during the review of the report on corporate governance and shareholding structure. Summary minutes of the Committee's meetings are drawn up and shall be signed by its members.

Remuneration Committee Meetings

In 2018, the Committee met nine times.

The meetings were preceded by discussions between members and/or prior individual review of documentation. The Committee did not make use of the services of external consultants.

In 2018, the members of the Committee took part in all nine meetings held.

The Parent Company's CEO attended the meetings during which the discussion of issues that concerned him was not on the agenda. Most meetings were attended by the Chairman of the Board Statutory Auditors and on one occasion also by other Standing Auditors.

***CEO and General Manager***

The CEO, as defined pursuant to art. 15 of the Articles of Association, is responsible for implementing strategic direction and business management, and makes use of the General Directorate.

With reference to personnel management, the CEO is responsible for:

- defining and ensuring implementation of the Group process for the management of employees;
- approving the personnel budget, in compliance with the organisational structure decided by the Board of Directors; the CEO also ensures that current and prospective measurements about the need for new professional profiles and sets of skills, in compliance with strategic decisions, are carried out.

The General Manager, as established by art. 17 of the Articles of Association, oversees implementation of the directives of management of the CEO and assists the latter in the execution of the resolutions of the Board of Directors. The General Manager is also responsible for submitting proposals to the CEO about the contents of the employee management process.

***Control Functions***

The corporate control functions cooperate, each according to its own area of responsibility, in order to ensure the adequacy of the remuneration and incentive policies as well as their compliance with applicable regulations, and their correct implementation.

Particularly:

- Compliance verifies, among other aspects, that the company remuneration system meets the objectives of complying with regulations, the Articles of Association, as well as any ethical codes and/or other standards of conduct applicable to the Group, so that the related legal and reputational risks are properly contained especially in relationships with customers;
- the Internal Audit function verifies, on a yearly basis, compliance of the remuneration practices with the approved policies and regulations. Any evidence and anomaly identified are brought to the attention of the relevant bodies and functions for the adoption of corrective measures and for the assessment of their significance in order to report them to the Bank of Italy. The outcomes of the assessments carried out are also reported to the Shareholders' Meeting on a yearly basis;
- the Risk Management function cooperates with the Remuneration Committee in order to guarantee that incentives complies with the risk appetite framework (RAF) and with the risk governance and management policies, and that they keep into account the level of capital and liquidity necessary to perform the activities undertaken. It also supports the Accounting function in determining, after the approval of the financial statements by the Shareholders' Meeting, the amount of the variable remuneration for the CEO, General Manager and other potential beneficiaries of the remuneration plans based on financial instruments, as well as during assessment of the conditions to be met for disbursing said remuneration.

***Other structures involved***

The main functions of the Parent Company involved in the preparation and implementation of the remuneration policy are:

- Human Resources;
- Strategic Planning and Management Control.

No external experts have participated in preparing the remuneration policy.

## *15.2 Connection between remuneration and performance*

***Non-Executives Directors***

The Shareholders' Meeting of 22 March 2016 set the rules for determining the remuneration of non-executive directors, including the members of the Remuneration Committee, and decided to pay each Director a fixed amount for each financial year to which a remuneration must be added for all Directors for each attendance at meetings of the Board of Directors, with the exception of the Chairman, Deputy Chairman and Chief Executive Officer. Reimbursement of expenses incurred in connection with their office is also provided.

The Shareholders' Meeting then requested the Board of Directors to determine additional remuneration for Directors who have held particular offices in accordance with Article 2389 of the Italian Civil Code for each of the years, also considering, where appropriate, company results, subject to a total amount calculated for each financial year, understood as including all fees awarded to members of the Board.

The non-executive Directors, including the Chairman, are not included in the recipients of the incentive mechanisms.

The respective Shareholders' Meetings of the subsidiary companies have resolved that the members of the Strategic Supervisory Bodies who play other roles within the Group as employees, do not receive any compensation for their role on the Board of Directors.

***CEO and General Manager***

The remuneration provided to the CEO and General Manager includes, in addition to a recurrent fixed amount, a variable amount (on a percentage basis), equal to 1,5% for the CEO and 0,75% for the General Manager, calculated on the consolidated results of the Bank, before taxes for the year, for the amount exceeding 80 million Euro, which is adjusted based on the ratio of the final Group[5] RORAC[6] to the prospective Group[7] RORAC, making sure that the variable component does not exceed the fixed remuneration.

***Control functions***

The remuneration package for key personnel belonging to the control function (Risk Manager, Compliance, Internal Audit, Anti-Money Laundering, Human Resources and Chief Financial Officer) is made up of a predominantly fixed component and a variable part which is attributed annually based on quality and efficiency criteria. In determining the compensation are in any case excluded incentive scheme mechanisms linked to the financial performance both of Banca IFIS and of the Group as a whole. The Heads of control functions are therefore excluded from any stock option plans. At least annually, the Remuneration Committee analyses the individual positions and, after hearing the CEO in reference to the department heads reporting to the latter:

- it expresses its opinion and submits any proposals to the Board of Directors regarding the key personnel of the control functions;
- it expresses its opinion and submit any proposals to the CEO regarding the key personnel of other internal control functions. Any decision taken is reported to the Board of Directors.

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[5] The reference period is the same as for the objective RORAC (ex-ante measurement).

[6] Indicator calculated as the ratio between Net Profit for the period and Capital Absorbed for first pillar risks. Elements that derive from extraordinary transactions will be disregarded from calculations, such as capital gains, corporate mergers, splits, acquisitions or any other non-recurring operation that the Board of Directors may decide on and that is likely to change the value of the indicator.

[7] Defined in the industrial plan with a 12-month horizon.

The assignment of the variable component is subject to a prior qualitative assessment on the achievement of the management objectives of the assigned projects and the quality of the service provided; the management and development of the assigned resources; the attention and prevention of risks in their areas of responsibility in addition to the management and coordination of the assigned activities. The percentage of the variable component to be recognised is measured on the basis of a scale of ratings, for which a percentage value is attributed to each of them. Therefore, it is possible to obtain 100% of the bonus if the evaluation is “Excellent”, 0% in the case of “Almost adequate or insufficient” rating. In any case the limit between fixed and variable amount cannot exceed the ratio of 1 to 3.

***Other key personnel***

For the rest of key personnel, the application of the variable component is subject to exceeding the minimum limits, as specified hereinafter, of the following quantitative parameters:

- the Group's consolidated result, before taxes for the financial year, being greater than € 80 million;
- compliance with the minimum regulatory limit in force for the Group's Liquidity Coverage Ratio (LCR) indicator identified on a quarterly basis in the reference year;
- compliance with the minimum regulatory limit in force for the Group's Net Stable Funding Ratio indicator identified quarterly in the reference year;
- the Consolidated Total Capital Ratio exceeding the Overall Capital Requirement communicated by the Supervisory Body under the “Decisions on capital” at the conclusion of the periodic supervisory review process (SREP).

The failure to comply with one of these parameters leads to the resetting of any variable remuneration.

The variable remuneration component is defined in advance for each single person, based on predefined criteria broken down into three areas:

- performance qualitative assessment, carried out by Top Management;
- achievement of a pre-set cost/income ratio;
- reaching specific economic, commercial and operating objectives and satisfying internal and external customers inclusive of corrective risk measures (MBO- Management by Objectives).

Once the bonus maximum theoretical amount is defined, it is broken down as follows:

| Key personnel categories | % max variable on previous year's gross annual salary | Top Management Assessment | Cost/income ratio | MBO |
|---|---|---|---|---|
| Executives with strategic responsibilities in charge of significant business units | *60%* | 20% | 20% | 60% |
| Business units | *80%* | 20% | 20% | 60% |

| | | | | |
|---|---|---|---|---|
| Risk management units | *50%* | 30% | 20% | 50% |
| Significant operating units | *50%* | 40% | 20% | 40% |
| Support, advisory and service units | *50%* | 50% | 20% | 30% |

The variable component will also recognised on condition that the recipient is still in post/an employee of the Group and not serving a period of notice for resignation or dismissal at the time of delivery. Payment of the variable component will also be suspended where disciplinary proceedings are in progress for fraud or gross negligence causing damage to the Bank or for behaviour that may lead to the individual's dismissal for just cause.

The Remuneration Committee has a final role in determining the remuneration criteria that are submitted for examination by the Board of Directors; it reports these decisions to the Remuneration Committee on an annual basis.

The Chief Executive Officer and the General Manager may define subsequent interventions on fixed and variable remuneration within the framework of the aforementioned criteria.

### *15.3 Main characteristics of the remuneration system for 2018 and information on share allocations*

The variable component of the remuneration for key personnel cannot exceed the 1:1 ratio with respect to the fixed remuneration and is determined on approval of the financial statements for the financial period ended 31 December of the previous year and is structured as follows:

- the portion to be deferred is 40%, 50% of which is paid in Banca IFIS S.p.A. shares that will be allocated after the 3-year vesting period and will be exercisable at the end of further one-year retention period set out. The remaining 50% is paid in cash at the end of the 3-year period and is annually reassessed at the statutory rate from time to time in force;
- the non-deferred variable component, equal to 60%, is paid 50% in cash while the remaining 50% in Parent Company shares will be exercisable at the end of the 3-year retention period, in line with the strategic planning scope.

The number of shares to be allocated is determined by taking the average market price in the month preceding the determination of variable component as being the share's fair value, to be carried out on the date of the Shareholders' Meeting to approve the financial statement.

In line with best market practices, the above rules apply to variable remuneration greater than 70,000 euros.

The portion of deferred variable remuneration is subject to the following malus mechanisms that may reduce, or even cancel, the previously determined ex-post amount, according to the criteria presented in the following table. These criteria are being checked in each of the three periods[8] ended subsequently to the determination of the variable component (accrual period).

| | | ***Group Consolidated Total Capital Ratio*** | | | |
|---|---|---|---|---|---|
| | | <11.38% | 11.38%< 12.38% | 12.38%< 13.38% | >13.38% |
| **Group RORAC** | ≥ 15% | -100.0% | --- | --- | --- |
| | 10.5%<< 15% | -100.0% | -30.0% | -20.0% | -10.0% |
| | < 10.5% | -100.0% | -40.0% | -30.0% | -20.0% |

The deferred variable component is also cancelled if the individual causes or contributes to causing:

- a significant loss for the Bank (equal to or exceeding 5% of the equity);
- violations of the obligations imposed under article 26, or when the subject is an interested party, of article 53, paragraphs 4 et seq., of the TUB/CBA or of obligations regarding remuneration and incentive schemes;
- fraudulent behaviour or misconduct to the detriment of the Bank.

Or, also, if:

- the Shareholders' Meeting has decided to revoke an office for just cause, that is, the Board of Directors has decided to terminate the employment contract for just cause.

On the occurrence of the conditions set out above, the Group can promote appropriate actions for the return of the variable component recognised and/or paid to key personnel, the claw back mechanism is applied even if the ratio of the Total Funds available[9] is lower than the regulatory threshold in force from time to time. These criteria are verified in each of the three financial years (accrual period) closed after the determination of the variable component and applied when the above conditions are met. In addition, an incentive that rewards excellent performance over time, *Long Term Incentive*, can be considered for business unit managers that record more than 20 million gross profit in the 2018 financial year. In essence, if in the three-year period 2018-2020 the previously established business results are achieved and the business unit managers receive a positive assessment from Top Management, the incentive will be implemented, defined ex-ante, not exceeding 60% of the individual manager's gross annual remuneration in the year 2020, in compliance with

[8] If these conditions are met in at least one of the three years of observation (accrual period), the corrective mechanisms listed in the table will be applied.

[9] EU Regulation no. 575/2013 (CRR) and Directive 2013/36/EU (CRD IV).

the maximum 1:1 ratio between fixed and variable amount, the value of which will be paid in Parent Company shares with a one year retention.

***Share-based remuneration plans***

Through resolution of 19 April 2018, shareholders approved a remuneration report and a remuneration plan based on the assignment of Banca IFIS shares for some company staff. The plan is described in the information document prepared pursuant to art. 114 bis of the TUF/CFA and its implementing rules (article 84 bis of the Issuer's Regulations) and was made available to the shareholders under the terms of law. In order to implement the above, with resolution of 7 March 2019, the Board of Directors approved granting of the variable component for the CEO and the General Manager with consequent application of the disclosure.

## *15.4 Ratio of the variable to fixed remuneration component*

| Key personnel categories | Maximum % bonus on the previous year's gross annual remuneration |
|---|---|
| Chief Executive Officer | 100% |
| General Manager | 60% |
| Executives with strategic responsibilities in charge of control functions | 33% |
| Head of control functions | 33% |
| Executives with strategic responsibilities in charge of significant business units | 60% |
| Business units | 80% |
| Risk management units | 50% |
| Significant operating units | 50% |
| Support, advisory and service units | 50% |

## *15.5 Non-monetary benefits*

Employees may receive some benefits, graded in relation to the business role and/or for service reasons, reflecting: healthcare policy, professional and extra-professional personal accident insurance, company car, official accommodation. To this end, it should be noted that following the company merger that occurred during 2018 a non-monetary benefit harmonisation process has begun, which has been partly completed with agreement of the auditors on 28 July 2017, on 28 March 2018 and on 12 December 2018. The attribution is summarised as follows: healthcare policy, professional and extra-professional personal accident insurance, permanent disability insurance, luncheon vouchers (for all employees – except some executives due to historical conditions not yet harmonised – with amounts ranging from € 5.20 to € 7.00), company car (recognised for some individuals based on current internal policies), company contributions to supplementary social security/pension plans (recognised for all employees, with permanent employment contracts, with percentages that vary from 1.5% to 5% calculated on gross annual remuneration and/or based on profit remuneration for TFR [severance indemnity] purposes, except for some previously acquired contracts). The above benefits, since they apply to all employees, are not considered discretional.

### *15.6 Implementation of Policies in subsidiaries*

**IFIS Finance Sp. z o.o.**

This document concerning the remuneration and incentive policies set up by the Parent Company applies to the subsidiary IFIS Finance Sp. z o.o., which is not required to draw up its own document in this regard.

The emoluments paid to directors and employees of the Polish subsidiary, IFIS Finance Sp. z o.o. are consistent with the parameters of the Group remuneration and incentive scheme.

**IFIS Leasing S.p.A., IFIS NPL S.p.A., IFIS Rental Services S.r.l., CAP.ITAL.FIN S.p.A., Credifarma S.p.A.**

During the 2018 financial year the following corporate transactions were carried out:

- acquisition of 100% of the company Cap.Ital.Fin S.p.A. on 2 February 2018 (date on which the transaction closed);
- merger by incorporation of IFIS Leasing S.p.A. carried out by a deed of merger signed on 15 May 2018, with effects ex-Article 2504 bis of the Italian Civil Code from May 28th;
- transfer by Banca IFIS S.p.A. in favour of the subsidiary IFIS NPL S.p.A., effective from 1st July 2018, of the business unit that deals with the activity of buying and managing distressed credit portfolios;
- acquisition of control of Credifarma S.p.A., the closing of which took place on 2 July last.

No fees are paid to members of the Board of Directors of any subsidiary, who are also employees of either Banca IFIS S.p.A. or its subsidiaries. In general, any fees for administrative or supervisory positions of employees of the Parent Company are expected to be paid by the latter.

The following tables summarise the data relating to aggregated remuneration broken down by lines of business in the Parent Company and in the subsidiaries.

***Table 29.a - Aggregated remuneration broken down by lines of business – Banca IFIS S.p.A.***

| *LINES OF BUSINESS* | NUMBER | TOTAL REMUNERATION |
|---|---|---|

| | | |
|---|---|---|
| BU Insurance | 2 | 36,205 |
| BU Corporate Finance | 6 | 610,914 |
| BU Tax Receivables | 26 | 1,490.463 |
| BU Commercial Credit | 343 | 16,856.743 |
| BU Pharmacy | 8 | 812,607 |
| BU International | 10 | 390,624 |
| BU Leasing | 193 | 5,672.845 |
| BU NPL - employees up to 30/06/2018 | 317 | 5,162.672 |
| BU Pharma | 15 | 886,265 |
| General Management – Control Functions | 481 | 5,257.417 |
| General Management – Staff and Support structures | 2 | 22,295,569 |
| Proprietary Finance | 2 | 101,402 |
| Special situations | 2 | 168,901 |
| TOTAL | 1,491 | 59,742,628 |

| Notes: |
|---|
| • - The information refers to employees of Banca IFIS S.p.A. in force as of 31/12/2018 (1,174 employees). The information relating to employees that are separated in IFID NPL S.p.A. relate to the period from 01/02/2018 to 30/06/2018 |
| ** - The "Control Functions" include no. 5 employees located at other companies in the Group |
| *** - The information on BU Leasing refers to the post merger period (from 28/05/2018 to 31/12/2018) |

| *Table 29.b. Aggregate quantitative information of IFIS NPL S.p.A.** | |
|---|---|
| **Number** | **TOTAL REMUNERATION** |
| **330** | **5,303,709** |

**Notes**:
* - The table considers the personnel in force as of 31/12/2018
The values are relative to the wages and salaries paid as of the company constitution date, 01/07/2018

***Table 29.c Aggregate quantitative information of IFIS Rental Services S.r.l.***

| Number | TOTAL REMUNERATION |
|---|---|
| **24** | **628,423** |

**Notes**:
* - The table considers the personnel in force as of 31/12/2018.
Values of wages and salaries available as of 01/06/2018.

| *Table 29.d Aggregate quantitative information of Credifarma S.p.A.** | |
|---|---|
| **Number** | **TOTAL REMUNERATION** |
| **40** | **1,736,709.00** |

**Notes**:
* - The table considers the personnel in force as of 31/12/2018.

| *Table 29.e Aggregate quantitative information of Cap.Ital.Fin S.p.A.** | |
|---|---|
| **Number** | **TOTAL REMUNERATION** |
| **45** | **1,273,832.62** |

**Note**:
* - The table considers the personnel in force as of 31/12/2018

The tables below show, in aggregate form, the main information on remuneration paid to “key personnel”. The amounts shown in the table are average gross amounts expressed in thousands of Euro.

*Table 30 – Aggregate information on remuneration by categories of key personnel*

**Aggregate Quantitative information of senior management and of remaining key personnel (employees only) at 31 December 2018 of Banca IFIS S.p.A. and IFIS NPL S.p.A.**

| **Fixed Component** | | | | | **Variable Remuneration** | | | | **Compensation details** | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Category of key personnel | Number of beneficiaries | Allowance | Compensation for special roles ex Art. 2389 of the Italian Civil Code | Fixed wages and salaries for employees | Bonuses and other incentives | Shares in profits | Non-monetary benefits | Other compensation | Total | Variable component in shares | Variable component in cash | Allocated sign-on and severance payments or for termination of employment contract | Approved sign-on and severance payments or for termination of the employment contract | Variable component of deferred remuneration allocated in the year 2018* | Variable component of the deferred remuneration allocated - accrued portion | Variable component of deferred remuneration - portion not yet accrued and not allocated | No. of persons with remuneration ≥ €1,000,000 |
| Senior Management | 2 | 25 | 650 | 308 | | 835 | 26 | - | 1,845 | 418 | 418 | - | - | 500 | 334 | 668 | 1 |
| Remaining key personnel | 43 | - | - | 5,065 | 1,584 | - | - | - | 6,649 | - | - | - | - | 159 | - | - | - |

*N.B. The values expressed in the table are values related to the total number of beneficiaries belonging to the individual categories of personnel.*

** There were no reductions in deferred remuneration recognized during the year due to performance corrections.*

The table below shows the total remuneration for each member of the Board of Directors and Senior Management, for the Banca IFIS Group.

The amounts shown in the table are expressed in thousands of Euro.

***Table 31** - Total remuneration for each member of the Board of Directors and Top Management – Banca IFS Group*

| Surname and name | Role | Company | Period in office | Total remuneration for the office in the period |
|---|---|---|---|---|
| | | | | |
| **Fürstenberg Sebastien Egon** | President of the Board of Directors | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 675 |
| **Csillaghy De Pacser Alessandro** | Vice President of the Board of Directors | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 525 |
| **Bossi Giovanni** | Chief Executive Officer | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 1,325 |
| **Benini Giuseppe** | Director | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 49 |
| **Benini Giuseppe** | Director | IFIS NPL S.p.A. | From 1/7/2018 to 31/12/2018 | 10 |
| **Benini Giuseppe** | Director | Credifarma S.p.A. | From 2/7/2018 to 31/12/2018 | 4 |
| **Maderna Francesca** | Director | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 42 |
| **Malinconico Antonella** | Director | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 49 |
| **Malinconico Antonella** | Director | IFIS NPL S.p.A. | From 1/7/2018 to 31/12/2018 | 10 |
| **Preve Riccardo** | Director | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 48 |
| **Salamon Marina** | Director | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 46 |
| **Santosuosso Daniele** | Director | Banca IFIS S.p.A. | From 1/1/2018 to 31/12/2018 | 45 |
| **Guerricchio Antonio** | Director | Credifarma S.p.A. | From 2/7/2018 to 31/12/2018 | 3.75 |

| | | | | |
|---|---|---|---|---|
| **Manna Maurizio** | President of the Board of Directors | Credifarma S.p.A. | From 2/7/2018 to 31/12/2018 | 18.93 |
| **Alessandrini Marco** | CEO (with reversibility of emoluments)* | Credifarma S.p.A. | From 2/7/2018 to 31/12/2018 | 3.3 |
| **Maciocchi Massimo** | CEO (with reversibility of emoluments)* | Credifarma S.p.A. | From 2/7/2018 to 31/12/2018 | 3.3 |
| **Magliocchetti Silvia** | CEO (with reversibility of emoluments)* | Credifarma S.p.A. | From 2/7/2018 to 31/12/2018 | 3.3 |
| **Staccione Alberto** | CEO (with reversibility of emoluments)* | Credifarma S.p.A. | From 2/7/2018 to 31/12/2018 | 3.3 |

# 16. LEVERAGE (ART. 451 CRR)

## Qualitative disclosure

As part of the Basel 3 regulatory framework, the leverage ratio was introduced, starting from 1 January 2015, as an additional requirement with respect to the risk-based capital requirements.

The inclusion of the leverage index in the regulatory framework meets the following objectives:

- restricting the expansion of overall exposures to the availability of an adequate capital base and containing, in the expansive phases of the economic cycle, the level of bank indebtedness, thus helping to reduce the risk of deleveraging processes in crisis situations;
- introducing an additional safeguard against model risk - through a simple non risk-based measure - with a backstop function for the risk-based capital requirement.

For the measurement of the leverage ratio, the Bank follows the method prescribed by the CRR Regulation - Part Seven and Circular no. 285/2013 for its application in Italy. Briefly, the indicator derives from the ratio of own funds for the component represented by the elements and instruments of Tier 1 capital and the size of the assets at risk of the Banking Group, on and off balance sheet, appropriately calibrated in application of specific conversion factors. For regulatory purposes, the measurement of the leverage ratio is carried out using IT procedures dedicated to the periodic production of statistical reports and consolidated prudential supervision. The leverage ratio is produced on a quarterly basis. The indicator is subject to monitoring both at individual and Banking Group level.

At regulatory level, the risk of financial leverage does not contribute to the definition of the total internal capital adequacy assessment process (ICAAP) performed annually by the Banking Group.

The risk of financial leverage is included in the RAF and therefore is subject to the procedures and control mechanisms included therein. The Leverage Ratio is one of the Key Risk Indicators monitored within the RAF for the year 2018; during 2018 it was approximately three times higher than the minimum EBA value of 3% coinciding with the Risk Capacity defined in the RAF.

For further information on the management processes followed by the Group, please refer to § 1.3.5 of this document.

## Quantitative disclosure

The leverage ratio is calculated according to the rules established by the “Commission Delegated Regulation (EU) 2015/62 of 10 October 2014 amending Regulation (EU) no. 575/2013 of the European Parliament and of the Council with regard to the leverage ratio”.

The present disclosure is also made in accordance with the provisions of the "Commission Implementing Regulation (EU) 2016/2005 of 15 February 2016 which establishes technical implementing rules regarding the disclosure on the leverage ratio of institutions pursuant to Regulation (EU) no. 575/2013 of the European Parliament and of the Council”.

The tables below show the financial leverage indicator at 31 December 2018 and the opening of the total exposure in the main categories, according to the provisions of articles 451(1)(a), 451(1) (b) and 451(1)(c) of the CRR. The amounts shown are related to the calculation of the leverage ratio in accordance with the current transitional provisions for reporting purposes.

The LRCom template below provides the opening of the exposures for the various reporting aggregates, the measurement of the Tier 1 Capital and the percentage value of the leverage ratio.

*Table 32 - LRCom Template - Harmonised disclosure on the leverage ratio*

| | | CRR leverage ratio exposures |
|---|---|---|
| | **On-balance sheet exposures (excluding derivatives and SFTs)** | |
| 1 | On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral guarantees) | 9,327,956 |
| 2 | (Asset amounts deducted in determining Tier 1 capital) | -204,844 |
| **3** | **Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets) (sum of lines 1 and 2) 16/2/2016 L 39/9 Official Journal of the European Union IT** | **9,123,112** |
| | **Exposures on derivatives** | |
| 4 | Replacement cost associated with all derivatives transactions (net of eligible cash variation margin) | 30,023 |
| 5 | Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method) | 1,686 |
| EU-5a | Exposure determined under Original Exposure Method | |
| 6 | Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the applicable accounting framework | |
| 7 | (Deductions of receivables assets for cash variation margin provided in derivatives transactions) | |
| 8 | (Exempted CCP leg of client-cleared trade exposures) | |
| 9 | Adjusted effective notional amount of written credit derivatives | |
| 10 | (Adjusted effective notional offsets and add-on deductions for written credit derivatives) | |
| **11** | **Total derivatives exposures (sum of lines 4 to 10)** | **31,709** |
| | **SFT exposures** | |
| 12 | Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions | |
| 13 | (Netted amounts of cash payables and cash receivables of gross SFT assets) | |
| 14 | Counterparty credit risk exposure for SFT assets | 51,272 |
| EU-14a | Derogation for SFTs: Counterparty credit risk exposure in accordance with Articles 429b(4) and 222 of Regulation (EU) No 575/2013 | 2,808 |
| 15 | Agent transaction exposures | |
| EU-15a | (Exempted CCP leg of client-cleared SFT exposure) | |
| **16** | **Total securities financing transaction exposures (sum of lines 12 to 15a)** | **54,080** |
| | **Other off-balance sheet exposures** | |
| 17 | Off-balance sheet exposures at gross notional amount 16/2/2016 L 39/10 Official Journal of the European Union IT | 1,127,015 |
| 18 | (Adjustments for conversion to credit equivalent amounts) | -583,150 |
| **19** | **Total other off-balance sheet exposures (sum of lines 17 and 18)** | **543,865** |
| | **(Exempted exposures in accordance with Articles 429 (7) and (14) of Regulation (EU) No. 575/2013 (on and off balance sheet))** | |
| EU-19a | (Intragroup exposures (solo basis) exempted in accordance with Article 429(7) of Regulation (EU) No. 575/2013 (on and off balance sheet)) | |

| | | |
|---|---|---|
| EU-19b | (Exposures exempted in accordance with Article 429 (14) of Regulation (EU) No. 575/2013 (on and off balance sheet)) | |
| | **Capital and total exposure measure** | |
| **20** | **Tier 1 capital** | **980,463** |
| **21** | **Leverage ratio total exposure measure (sum of lines 3, 11, 16, 19, EU-19a and EU-19b)** | **9,752,766** |
| | **Leverage ratio** | |
| **22** | **Leverage ratio** | **10.05%** |
| | **Choice on transitional arrangements and amount of derecognised fiduciary items** | |
| EU-23 | Choice on transitional arrangements for the definition of the capital measure | |
| EU-24 | Amount of derecognised fiduciary items in accordance with Article 429(11) of Regulation (EU) No 575/2013 | |

The LRSum template below provides a reconciliation of the total exposure (indicator denominator) and the financial statements values.

***Table 33 - LRSum template - Summary of reconciliation of accounting assets and leverage ratio exposures***

| | | **Applicable amounts** |
|---|---|---|
| 1 | Total assets as per published financial statements | 9,382,261 |
| 2 | Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation | 26,990 |
| 3 | (Adjustment for fiduciary assets recognised on the balance sheet pursuant to the applicable accounting framework but excluded from the leverage ratio total exposure measure in accordance with Article 429, paragraph 13, of Regulation (EU) no. 575/2013) | |
| 4 | Adjustments for derivative financial instruments | 4,494 |
| 5 | Adjustment for securities financing transactions (SFTs) | |
| 6 | Adjustment for off-balance sheet items (conversion to credit equivalent amounts of off-balance sheet exposures) | 543,865 |
| EU-6a | (Adjustment for intragroup exposures excluded from the leverage ratio total exposure measure in accordance with Article 429, paragraph 7, of Regulation (EU) no. 575/2013) | |
| EU-6b | (Adjustment for exposures excluded from the leverage ratio total exposure measure in accordance with Article 429, paragraph 14, of Regulation (EU) no. 575/2013) | |
| 7 | Other adjustments | -204,844 |
| **8** | **Leverage ratio total exposure measure** | **9,752,766** |

The LRSpl templates provides the breakdown of exposures other than derivatives and SFTs by counterparty.

***Table 34 - LRSpl template - Split-up of on-balance sheet exposures (excluding derivatives, SFTs and exempted exposures)***

| | | **CRR leverage ratio exposures** |
|---|---|---|
| EU-1 | Total on-balance sheet exposures (excluding derivatives, SFTs and exempted exposures), of which: | 9,327,956 |
| EU-2 | Trading book exposures | |
| EU-3 | Banking book exposures, of which: | 9,327,956 |
| EU-4 | Covered bonds | |
| EU-5 | Exposures treated as sovereigns | 1,349,738 |
| EU-6 | Exposures to regional governments, MDB, international organisations and PSE not treated as sovereigns | 603,613 |
| EU-7 | Institutions | 314,022 |
| EU-8 | Secured by mortgages on immovable property | 131,801 |
| EU-9 | Retail exposures | 1,139,363 |
| EU-10 | Corporate | 3,577,352 |
| EU-11 | Exposures in default | 1,495,320 |
| EU-12 | Other exposures (e.g. equity, securitisations, and other non-credit obligation assets) | 716,747 |

# 17. USE OF CREDIT RISK MITIGATION TECHNIQUES (ART. 453 CRR)

**Qualitative disclosure**

The strategies pursued by the Banking Group require credit lines to be preferably backed by suitable guarantees and risk mitigation instruments.

The guarantees for their ability to split the credit risk, if managed in an integrated manner with the knowledge of the customer, become the main and most effective instrument for the effective mitigation of the risk.

The Banca IFIS Group has implemented the requirements of Regulation (EU) 575/2013 for the purpose of recognising the effects of credit risk mitigation produced by the presence of collateral and personal guarantees for the protection of credit.

The process of controlling the acquisition of guarantees and the use of credit risk mitigation techniques focuses on the definition of suitable controls, instruments and processes aimed at guaranteeing firstly the verification of alignment with Supervisory requirements, distinguishing between:

- “general requirements”, such as legal certainty, the speed of implementation and organisational requirements;
- “specific requirements”, with particular attention to the revaluation and monitoring of the value of the guarantees and the verification of the absence of a significant correlation between the debtor's ability to repay/creditworthiness and the guarantee.

The continuous verification of the quality and adequacy of the guarantees assessment procedures is carried out by the Bank's Risk Management function, with the aim of supervising, on a centralised basis, the process for assessing and monitoring the guarantees acquired on the receivables portfolio of the Banca Group IFIS. For greater operational effectiveness, these processes are carried out by a dedicated organisational unit, recently established, called “Collateral Monitoring”, which reports directly to the Bank's Chief Risk Officer.

For further information on the management processes followed by the Group, please refer to § 1.3.2 of this document.

<u>Compensation policies and processes</u>

The Bank does not apply processes for offsetting credit risk exposures with counter entries in the balance sheet or “off-balance sheet”.

<u>Main types of guarantors and counterparties in credit derivative transactions and their creditworthiness</u>

The Banking Group has no credit derivative transactions.

Information on concentrations of market or credit risk within the credit risk mitigation instruments adopted

There are no concentration levels of significant risks within the credit risk mitigation instruments adopted.

**Quantitative information**

In this Section the guaranteed exposure amounts are shown according to the provisions of articles 453(f) and 453(g) of the CRR, with reference to the situation as of 31 December 2018.

***Table 35 - Breakdown of exposures by regulatory class***

| *Portfolios* | Collateral guarantees | Personal guarantees | Total |
|---|---|---|---|
| Central governments and central banks | 77,573 | 0 | 77,573 |
| Regional governments or local authorities | 0 | 0 | 0 |
| Public sector bodies | 0 | 0 | 0 |
| Supervised intermediaries | 0 | 0 | 0 |
| Companies and other bodies | 6,865 | 0 | 6,865 |
| Retail exposures | 0 | 0 | 0 |
| Exposures guaranteed by real estate | 131,801 | 0 | 131,801 |
| Exposures in default | 0 | 0 | 0 |
| Exposures to collective saving investment entities (O.I.C.R.) | 0 | 0 | 0 |
| Equity exposures | 0 | 0 | 0 |
| Other exposures | 0 | 0 | 0 |
| **Total** | **138,666** | **-** | **138,666** |

## 18. INTRODUCTION OF IFRS 9 (ART. 473 bis CRR)

**Qualitative information**

Starting from 1 January 2018, the Group has adopted the new accounting standard "IFRS 9 Financial Instruments" (so-called IFRS 9).

With reference to the introduction of IFRS 9, on 12 December 2017, the European Parliament issued Regulation (EU) 2017/2395, which updates the CRR, inserting the new article 473 bis, "Introduction of IFRS 9", which offers the option for banks to mitigate the impacts on own funds resulting from the introduction of the new accounting standard; in particular, the transitional provisions define the option for institutions of including in their Tier 1 capital a portion of the accrued provisions for expected credit losses, in application of IFRS 9 and up to the end of the transitional period (1 January 2018 / 31 December 2022).

In this regard, Banca IFIS has informed the Bank of Italy of their decision to apply the transitional provisions for the entire period. Inclusion in CET1 will take place gradually by applying the following factors:

- 95% from 1 January 2018 to 31 December 2018;
- 85% from 1 January 2019 to 31 December 2019;
- 70% from 1 January 2020 to 31 December 2020;
- 50% from 1 January 2021 to 31 December 2021;
- 25% from 1 January 2022 to 31 December 2022.

Regulation (EU) 2017/2395 also governs the disclosure obligations that institutions are required to publish, providing to the EBA the issuance of specific guidelines on the subject. Upon implementation of the regulations, on 12 January 2018 the EBA issued specific guidelines which stipulate that banks that adopt a transitional treatment with reference to the IFRS9 impact are required to provide a comparison of own funds and capital and leverage ratios with and without the application of the related transitional provisions.

**Quantitative information**

The application of IFRS 9 at the time of the First Time Adoption (FTA) on 1 January 2018 did not result in an increase in provisions for expected credit losses; therefore the transitional provisions – "static approach" – are not applicable.

On 31 December 2018, the application of IFRS 9 led to an increase in provisions for expected credit losses of € 462 thousand, net of the tax effect. Therefore, in application of the transitional provisions – "dynamic approach" – the sum of € 222 thousand – attributable to the Group – was recognised in the Tier 1 capital (CET1).

*Table 36 - Comparison of own funds, capital ratios and leverage with and without the application of transitional provisions for IFRS 9*

| | | **31/12/2018** |
|---|---|---|
| | **Available capital (amounts)** | |
| 1 | Common Equity Tier 1 capital (CET1) | 924,285 |
| 2 | Common Equity Tier 1 capital (CET1) as if the transitional provisions regarding IFRS9 or similar expected credit losses had not been applied | 924,063 |
| 3 | Tier 1 capital | 980,463 |
| 4 | Tier 1 capital (CET1) as if the transitional provisions regarding IFRS9 or similar expected credit losses had not been applied | 980,241 |
| 5 | Total capital | 1,257,711 |
| 6 | Total capital as if the transitional provisions regarding IFRS9 or similar expected credit losses had not been applied | 1,257,489 |
| | **Risk-weighted assets (amounts)** | |
| 7 | Total risk-weighted assets | 8,974,645 |
| 8 | Total risk-weighted assets as if the transitional provisions regarding IFRS9 or similar expected credit losses had not been applied | 8,974,328 |
| | **Capital ratios** | |
| 9 | Common Equity Tier 1 capital (as a percentage of the risk exposure amount) | 10.30% |
| 10 | Common Equity Tier 1 capital (as a percentage of the risk exposure amount) as if the transitional provisions regarding IFRS9 or similar expected credit losses had not been applied | 10.30% |
| 11 | Tier 1 capital (as a percentage of the risk exposure amount) | 10.92% |
| 12 | Tier 1 capital (as a percentage of the risk exposure amount) as if the transitional provisions regarding IFRS9 or similar expected credit losses had not been applied | 10.92% |
| 13 | Total capital (as a percentage of the risk exposure amount) | 14.01% |
| 14 | Total capital (as a percentage of the risk exposure amount) as if the transitional provisions regarding IFRS9 or similar expected credit losses had not been applied | 14.01% |
| | **Leverage ratio** | |
| 15 | Measurement of the total exposure of the leverage ratio | 9,752,766 |
| 16 | Leverage ratio | 10.05% |
| 17 | Leverage ratio as if the transitional provisions regarding IFRS9 or similar expected credit losses had not been applied | 10.05% |

# 19. ADEQUACY OF RISK MANAGEMENT MEASURES AND RECONCILIATION BETWEEN OVERALL RISK PROFILE AND CORPORATE STRATEGY (ART. 435 e) and f))

With reference to the requirements of article 435 – paragraph 1, letters e) and f) of Regulation (EU) no. 575/2013, a summary disclosure on the adequacy of the risk management measures and the reconciliation between the overall risk profile and the corporate strategy is provided below. For more details, reference should be made to paragraphs 1.2 "*Risk profile and risk measurement and management systems*" and 1.3 "*Strategies and processes for risk management*".

***Risk management measures adequacy***

The Banca IFIS Group carries out continuous updating activities in relation to the systems and processes used in order to improve its risk management system.

The Risk Management function has the task of ensuring protection and the integrated management of risks by ensuring the development and improvement of measurement methods and models.

For appropriate risk management, the Group's internal control system plays a key role to ensure proper disclosure and suitable audit coverage of all activities and, in particular, in the areas featuring greater corporate risk. Audits involve, with different roles, the Corporate Bodies of the Group companies, the Parent Company's Management and the Group's personnel. One of the main players of the internal control system is the Control and Risks Committee whose task is to support the assessments and decisions taken by the Board of Directors.

***Reconciliation between the overall risk profile and the corporate strategy***

The Group ensures full compliance with and a precise reconciliation among: the business model, the strategic plan, the Risk Appetite Framework (RAF), the capital adequacy assessment process (ICAAP), the liquidity management process (ILAAP), the budgets, the company's organisation and the internal control system. The RAF is the reference framework governing the risk appetite, the tolerances thresholds and the risk limits, in line with the business model and the strategic plan.

The processes of RAF definition and strategic planning are highly interrelated, since both are based on assumptions of correct profitability for risk, capital strength and solidity in terms of liquidity.

The RAF definition criteria take account of the business model and reference markets in which the Group operates, the strategic objectives, and an integrated view of the risks measured in accordance with the procedure adopted for ICAAP and ILAAP purposes.

Risk appetite is measured at Group level and is expressed through indicators representing the strategic and financial objectives of the Group and the regulatory constraints consistently with verification of the adequacy of capital and liquidity with the risk management processes.

Such indicators are defined based on specific significant risks for the bank and specific business units and are mainly attributable to the capital amount and adequacy, liquidity, profitability and asset quality. These indicators are regularly monitored by the Risk Management function and the relevant disclosure is provided to the bodies responsible for management and strategic supervision. In addition to the strategic indicators defined in the RAF, a further set of risk indicators is monitored.

Due to the specific business model adopted, the main risk to which the Group is exposed is credit risk.

Operational risk, being a cross-sectional risk that can potentially involve all structures and business of the Bank, is considered as a significant risk for the Group. The model risk is also of importance, due to the significant incidence and number of valuation models operating in the non-performing loans segment acquired from third parties (IFIS NPL and FBS subsidiaries).

Finally, with regard to liquidity risk, this potentially affects a large part of the Bank's operating units and is significant for all credit institutions and the Supervisory Authority. In order to ensure correct management of liquidity risk, a set of indicators (LCR, NSFR and Maturity Ladder) is regularly monitored. Monitoring also involves the business units that can generate inflows and outflows , as well as the duration of assets and liabilities.

The types of risks of medium significance, which relate to the Banking Group, refer to concentration risk, reputational risk, the risk associated with the portion of encumbered assets, strategic risk and interest rate risk.

Other types of risk are also marginal, such as market risk, counterparty and credit valuation adjustment risk, country and transfer risk, Italy sovereign risk, residual risk, settlement and delivery risk, risk arising from securitisation transactions, risk arising from investments and excessive leverage risk.

## 20. CEO'S DECLARATION PURSUANT TO ART. 435, LETTERS E) AND F) OF REGULATION (EU) NO. 575/2013

Pursuant to art. 435, paragraph 1, letters e) and f) of Regulation 575/2013 (CRR), the CEO, Giovanni Bossi, vested with the relevant powers by the Board of Directors, declared that:

- the risk management systems put in place by the Banca IFIS Group and described in the "Public Disclosure at 31 December 2018 – Pillar 3" document, are in line with the Group's profile and strategy;
- in the above-mentioned document, approved by the Parent Company's Board of Directors, the Group's overall risk profiles are described and these are consistent and in line with the business strategy.

Venice, 7th March 2019

The CEO

Giovanni Bossi

## 21. DECLARATION OF THE CORPORATE CHIEF FINANCIAL OFFICER

Pursuant to Article 154 bis, Paragraph 2 of Italy's "Consolidated Law on Financial Intermediation", the Corporate Chief Financial Officer of Banca IFIS S.p.A., Mariacristina Taormina, declares that the accounting information contained in this "Public Disclosure at 31 December 2018 – Pillar 3" corresponds to the company's accounting records, books and entries.

Venice, 7th March 2019

The Corporate Chief Financial Officer

Mariacristina Taormina