UniCredit Bank

# BASEL III PILLAR 3 DISCLOSURE REPORT

according to

NBR Regulation no. 5 / 20.12.2013
regarding prudential requirements for credit institutions

and

Regulation no. 575 / 2013 of European Parliament and Council dated 26.06.2013 regarding prudential requirements for credit institutions and investment companies and amending Regulation (UE) no.648 / 2012

**Report reference date: 31st December, 2016**

**Cuprins**


1. GENERAL INFORMATION REQUIREMENT .......... 3
   1.1. INTRODUCTION-RISK MANAGEMENT OBJECTIVES AND POLICIES .......... 3
   1.2. PILLAR II RISKS AND INTEGRATION OF RISKS .......... 4
   1.3. OTHER RISKS .......... 5
   1.4. REPORTING .......... 6
   1.5. TOP AND EMERGING RISKS .......... 6
   1.6. RISK MANAGEMENT CULTURE .......... 7
   1.7. RISK MANAGEMENT AND BUSINESS MODEL .......... 7
2. SCOPE OF APPLICATION .......... 11
   2.1. RELEVANT SCOPE OF CONSOLIDATION .......... 11
   2.2. ENTITIES DEDUCTED FROM OWN FUNDS .......... 12
   2.3. ENTITIES ADDED TO RWA .......... 12
   2.4. DESCRIPTION OF THE UNICREDIT GROUP COMPOSITION IN ROMANIA AND CONSOLIDATION METHODOLOGY .......... 12
   2.5. SUBSTANTIAL OR LEGAL IMPEDIMENTS THAT HINDER THE RAPID TRANSFER OF CAPITAL RESOURCES WITHIN THE GROUP .......... 14
3. OWN FUNDS .......... 17
   3.1. REGULATORY CAPITAL - SUMMARY RECONCILIATION AND CHANGES OVER TIME .......... 17
4. CAPITAL REQUIREMENTS .......... 20
   4.1. GENERAL COMMENT .......... 20
   4.2. CAPITAL STRENGTHENING .......... 22
   4.3. RECLASSIFICATION OF FINANCIAL ASSETS TABLE .......... 22
   4.4. RISK MANAGEMENT AND BUSINESS MODEL - RWA SEGMENTATION .......... 22
   4.5. RWAS AND BUSINESS ACTIVITIES .......... 23
   4.6. CAPITAL SURCHARGES & BUFFERS .......... 23
   4.7. CAPITAL PLANNING- TARGETED LEVEL OF CAPITAL .......... 23
   4.8. RWA CALCULATION METHOD AND MODELS .......... 23
   4.9. RWA CHANGES OVERTIME .......... 24
5. CREDIT RISK .......... 24
   5.1. RISK MANAGEMENT ORGANIZATION .......... 24
   5.2. ASSETS & LIABILITIES BY RESIDENTIAL CONTRACTUAL MATURITY .......... 26
   5.3. CREDIT RISK PROFILE AND CONCENTRATIONS .......... 27
   5.4. CREDIT RISK IMPAIRED/NLPS POLICIES .......... 34
   5.5. STRESS TESTING DISCLOSURE .......... 35
   5.6. CREDIT RISK IMPAIRED/NLPS OPENING VS CLOSING BALANCES .......... 35
   5.7. RWA CALCULATION METHOD AND MODELS .......... 37
   5.8. RWA - IRB BY INTERNAL RATING GRADE .......... 38
   5.9. RWA – BACKTESTING .......... 39
   5.10. CREDIT RISK MITIGATION .......... 39
6. EXPOSURE TO COUNTERPARTY RISK .......... 41
   6.1. LIMITS ON EXPOSURES, POLICIES FOR ASSESSING COUNTERPARTY CREDIT RISK AND GUARANTEE RISK, MANAGEMENT OF WRONG - WAY RISK ETC. .......... 41
   6.2. POSITIVE FAIR VALUE OF FINANCIAL AND CREDIT DERIVATIVES, COLLATERAL HELD, VALUE OF CCF ETC. 42
7. MARKET RISKS .......... 43
   7.1. PRICE RISK, INTEREST RATE RISK, EXCHANGE RATE RISK AND CREDIT SPREAD - TRADING BOOK .......... 43

7.2. PRICE RISK, INTEREST RATE RISK, EXCHANGE RATE RISK - BANKING BOOK ........ 44
7.3. STRESS TESTING DISCLOSURES ........ 45
7.4. RWA CALCULATION METHOD AND MODELS ........ 47
7.5. RISK MANAGEMENT ORGANIZATION ........ 47

**8. OPERATIONAL RISK ........ 48**

8.1. RISK MANAGEMENT ORGANIZATION ........ 48
8.2. STRESS TESTING DISCLOSURES ........ 51
8.3. RWA CALCULATION METHOD AND MODELS ........ 51
8.4. OTHER RISKS - RISK TYPES AND RISK MANAGEMENT ........ 51
8.5. OTHER RISKS - PUBLICLY KNOWN RISK EVENTS ........ 52

**9. EQUITY EXPOSURES ........ 53**

9.1. DESCRIPTION OF THE BANK'S PARTICIPATIONS AND DESCRIPTION OF THE METHOD OF BOOKING ........ 53

**10. INTEREST RATE RISK ON POSITIONS IN THE BANKING BOOK ........ 53**

10.1. SCENARIOS USED TO MEASURE AND MANAGE INTEREST RATE RISK, QUANTIFICATION OF THE IMPACT ON THE BANKING BOOK OF AN INTEREST RATE SHOCK ........ 53

**11. FINANCIAL INVESTMENT RISK ........ 54**

11.1. DESCRIPTION OF FINANCIAL INVESTMENT RISK ........ 54

**12. REAL ESTATE RISK ........ 54**

12.1. DESCRIPTION OF REAL ESTATE RISK ........ 54

**13. BUSINESS RISK ........ 54**

13.1. DESCRIPTION OF BUSINESS RISK ........ 54

**14. STRATEGIC RISK ........ 55**

14.1. DESCRIPTION OF STRATEGIC RISK ........ 55

**15. REPUTATIONAL RISK ........ 55**

15.1. DESCRIPTION OF REPUTATIONAL RISK ........ 55

**16. EXCESSIVE LEVERAGE RISK ........ 56**

16.1. DESCRIPTION OF EXCESSIVE LEVERAGE RISK ........ 56

**17. LIQUIDITY RISK ........ 57**

17.1. LIQUIDITY ........ 57
17.2. FUNDING (ASSET ENCUMBRANCE) ........ 61
17.3. LIQUIDITY BUFFER AND FUNDING STRATEGY ........ 63

**18. REMUNERATION POLICY ........ 64**

18.1. DESCRIPTION OF REMUNERATION POLICY ........ 64

**19. ANNEX 1: BASEL II PILLAR 3 DISCLOSURE FOR UNICREDIT CONSUMER FINANCING SA ........ 69**

**20. ANNEX 2: BASEL II PILLAR 3 DISCLOSURE FOR UNICREDIT LEASING IFN ........ 81**

UniCredit Bank

# 1. General information requirement

## *1.1. Introduction-Risk management objectives and policies*

Risk management objectives are correlated with the Banks' general strategic objectives:

- Adequate and prudent management of risks and in particular of significant risks;
- Selective enlargement of the loan book, by achieving a balanced structure on client segments;
- Products' diversification;
- Conservation of a sustainable profitability threshold;
- Mitigation – to the possible extent – of the negative impact generated by the economic crisis;
- Identification of optimal solutions for the clients who are confronted with the negative effects of the financial crisis;
- Adequate training of the personnel, so that they may offer high quality services to customers;
- Local integration of the existent standards at the group's level under the form of internal regulations and procedures.
- The Bank's strategic objectives include the development of a sound risk culture extended both at management level and at the level of all business units with risk management responsibilities, by determining firm-wide views on acceptable relationships between the risks and profitability at a Bank's overall level and for each significant activity in order to ensure sustainability of sound and prudent operations.

Risk management within the Bank includes:

- A risk management culture;
- A risk management framework;
- A policy for new product appproval.

Risk management is a priority of UniCredit Bank's management, being considered as an essential and mandatory condition in ensuring the Bank stability and performance. Risk management function actively is involved in the development of strategy for significant risk management of the Bank and decisions regarding risk management, providing a complete picture of the full range of risks to which the credit institution is exposed.

Risk management involves identifying, assessing, measuring, monitoring and controlling or reducing the risks, so that it ensures the alignment to the principles in the Bank's general policy on significant risk management.

The risk management function is actively involved in the approval of new products or in the implementation of significant changes to existing products having a clear overview of the roll-out of new products (or significant changes to existing products) across different business lines and portfolios and monitors that changes to existing products go through the formal approval process of new products.

The regulations and processes that the Bank has implemented correspond to the overall strategy being correlated with the level of own funds and the Bank's experience in risk management, as well as with the level of risk adjusted exposure set by the Bank management.

Risk management processes involve techniques for quantifying and monitoring risks which are based on a set of principles for risk management harmonized with the best international practices.

The risks assessment and identification is a permanent process within the Bank at both individual level (transaction / debtor) and at global level (portfolio). Risks identification and assessment is performed based on the analysis of internal and external factors that can negatively affect or endanger the accomplishment of UniCredit Bank's strategic objectives.

For entitities directly controlled, taking into account the specific of their activities, the aim is to implement processes for risk identification, management, monitoring and reporting, and internal control mechanisms in order to ensure that these systems, processes and mechanisms are consistent and well-integrated at Group level.

### *1.2. Pillar II risks and integration of risks*

The Internal Capital Adequacy Assessment Process ("ICAAP") focuses on the development and maintenance of sound internal procedures and systems which allow the evaluation of the bank capital adequacy, i.e. the balance between the assumed risk (measured in terms of Internal Capital – "IC") and the available capital (Available Financial Resources – "AFR"), both related to the current situation and in a forward looking perspective, as represented by the budget and strategic plan.

The comparison between AFR and IC is the Risk Taking Capacity (RTC), a key metric included in the Risk Appetite framework.

ICAAP is an integral part of management and decision-making processes. In this context, the main impacts are related to the risk awareness embedding in the strategic planning and budgeting processes, limit setting and performance evaluation according to a backward and forward-looking perspectives. Setting up an appropriate capital adequacy process means not only using internally developed metrics, but also setting the appropriate capital levels corresponding to the Pillar 1 metrics, such as the Core Tier 1 (CT1) and Total capital ratios as banks are expected to operate with a capital level higher than minimum requirements (i.e. Regulatory Capital).

The process consists of following phases:

- Perimeter definition and risk identification and mapping
- Risk profile assessment and stress testing
- Risk appetite setting and Capital allocation
- Monitoring and reporting

The process of identification and assessment of significant risks is an element of internal control and aims to ensure that internal control objectives are met (efficiency, information and conformity objectives).

UniCredit Bank carries out an analysis by selecting which risks are relevant with reference to its perimeter of activities.

The risk definition and mapping is not a one-off process, but it is done on an on-going basis to improve the risk management framework according to the international best practices and to update the analysis of UCB according to the business evolution.

UCB reviews the risk map and classification according to the proportionality principle, at least on an annual base and in case of relevant changes. The risk map is the basis for the risk evaluation and measurement.

### *1.3. Other risks*

Other risks considered to have major impact on the bank patrimony are the risks associated with outsourcing activities .

The management of outsourcing activities risk takes into consideration, in a non exhaustive form:

1. Reputation, operational and financial impact on the Bank that can be generated by the execution/failure to execute accordingly the contract obligations by the supplier;
2. Consequences of outsourcing and their impact upon the assurance of the respect by the Bank of the legal framework and internal regulations framework;
3. Impact upon Bank's clients or upon counterparties in case of default in the execution of contract obligations by the supplier;
4. Analysis of supplier's solvency taking into consideration: reputation, previous experience in the field, quality of services, internal control framework regarding their activities and performance, quality and quantity of resources at the disposal of the supplier for the execution of activities subject to contract, confidentiality of data/ processed transactions etc.;
5. Outsourcing relationships will be governed by contracts; the contracts will include clear provisions regarding the nature of the outsourced activity, the responsibilities of the Bank and of the supplier, as well as activities control tools etc.;
6. For each activity proposed for outsourcing an analysis and opinion will be required from the departments directly involved in risk analysis, such as: Risk Division, Legal and Compliance Department, as well as other units in case the outsourced activity represents their work area;
7. A cost-benefit analysis on outsourced activities is assessed;

8. Degree to which the Bank and the control authorities have access to information, files and databases of the supplier that are a result of the contractual obligations;
9. Back-up plans or measures to remediate crisis situations; they must take into consideration any event that can impose/ force the termination of the contractual relationship and – as the case may be the transfer under optimal circumstances of the activity to another supplier or its takeover by the Bank.

### *1.4. Reporting*

Capital adequacy evaluation is a dynamic process that requires a regular monitoring to support the decision-making process. Further to the monitoring, a strong and proper communication process is in place, both for management purposes and disclosure to external stakeholders.

As per local requirements, of Unicredit Bank and Legal Entities belonging to the UCB Group have to provide the National Bank of Romania, an annual report, regarding the internal capital adequacy assessment process, in compliance with the provisions set out in NBR Regulation 5/2013 article 69, including the identification of aspects needing improvement and measures planned to that end at the credit institution level.

### *1.5. Top and emerging risks*

The risk management framework is clearly and transparently transposed in internal norms, procedures, manuals and codes of conduct, distinctively mentioning the standards applicable for all employees and those applicable only to specific categories of employees.

Based on the Group's approach and on the internal analysis performed with the Group guidance, UniCredit Bank S.A. identified the following significant risks:

1. Credit risk
2. Market risk
3. Liquidity risk
4. Operational risk
5. Reputational risk
6. Business risk
7. Financial investment risk
8. Real estate risk
9. Strategic risk
10. Risk of excessive leverage.

11. Inter-concentration risk

### *1.6. Risk Management culture*

The Bank develops a risk culture which is integrated and defined institution-wide, being based on a full understanding of the risks faced by the Bank and on how they are managed, taking into account Bank's risk tolerance/ appetite.

Risk management responsibilities are not confined to risk specialists or control functions, as each Bank's employee has to be fully aware of his/her own responsibilities with regard to risk management. Business units are primarily responsible for managing risks on a day-to-day basis, taking into account the Bank's risk tolerance/ appetite and in line with internal policies, procedures and controls.

The Bank's strategic objectives include the development of a sound risk culture extended both at management level and at the level of all business units with risk management responsibilities, by determining firm-wide views on acceptable relationships between the risks and profitability at a Bank's overall level and for each significant activity in order to ensure sustainability of sound and prudent operations.

The Banks aims to develop a holistic framework for the management of significant risks – credit risk, market risk, operational risk, liquidity risk, reputational risk, business risk, financial investment risk, strategic risks and real estate investment risk, risk of excessive leverage and inter-concentration risk – taking into account the correlations and interdependences between different risk types.

The Bank is finally responsible for risk assessment, as it critically assess the risks and does not solely rely on external evaluations.

### *1.7. Risk Management and business model*

The internal control framework is based on the 3 lines of defense model:

- The first line of defense is represented by the risk management processes established in the Bank in order to identify, measure or assesses, monitor, manage and report risks. Risk management responsibilities are not confined to risk specialists or control functions, as each Bank's employee has to be fully aware of his/her own responsibilities with regard to risk management. Business units are primarily responsible for managing risks on a day-to-day basis, taking into account the Bank's risk tolerance/appetite and in line with internal policies, procedures and controls.
- The second line of defense is represented by risk management and compliance functions, that ensure effective and efficient operations, adequate control of risks, prudent conduct of business, reliability of financial and non-financial information reported, both internally and externally, and compliance with laws, regulations, supervisory requirements and the Bank's internal policies and procedures.

- The third line of defense is represented by internal audit function, which ensures an independent assessment of the compliance of all activities and business units of the Bank (including the risk management function and compliance function) with its policies and procedures. The internal audit function also assesses whether existing policies and procedures remain adequate and comply with legal and regulatory requirements.

Internal control framework covers the overall Bank organization, including the activities of all business, support and control units.

Internal control function within the Bank includes the following independent specific control functions:

- Risk management function
- Compliance function
- Internal audit function

*Risk management organisation, processes and key functions*

The risks management structure is based on several operational and control functions, defined as per the provisions of the Bank Organizational and Functioning Regulation and the existent Group-level provisions.

The risk management framework in the Bank is based on the following components:

- The risk management processes established in the Bank in order to identify, measure or assesses, monitor, manage and report risks. Risk management responsibilities are not confined to risk specialists or control functions, as each Bank's employee has to be fully aware of his/her own responsibilities with regard to risk management. Business units are primarily responsible for managing risks on a day-to-day basis, taking into account the Bank's risk tolerance/appetite and in line with internal policies, procedures and controls.
- The risk management and compliance functions, that ensure effective and efficient operations, adequate control of risks, prudent conduct of business, reliability of financial and non-financial information reported, both internally and externally, and compliance with laws, regulations, supervisory requirements and the Bank's internal policies and procedures.
- The internal audit function, which ensures an independent assessment regarding the compliance of all activities and business units of the Bank (including the risk management function and compliance function) with policies and procedures of the Bank. The internal audit function also assesses whether existing policies and procedures remain adequate and comply with legal and regulatory requirements.

The organizational structures with responsibilities on risk management are Supervisory Board and Management Board, and also internal specialised committees.

In order to ensure an adequate risk management framework, the Bank organised the Risk Management Committee at Supervisory Board level and also the Operative Risk Management Committee.

The Risk Management Committee at Supervisory Board has a consultative function for the decisions of the management body regarding the risk appetite and global strategy for the management of the current and future risks the Bank is exposed to and assist the Supervisory Board in overseeing the implementation of that strategy by senior management.

The Operative Risk Management Committee organized at Management Board level has a consultative function for Management Board with regard to any actions to ensure a rigorous and adecquate risk management framework.

During 2016, the Risk Management Committee at Supervisory Board level had 2 meetings, and the Operative Risk Management Committee had 4 meetings.

Also, an important role in risk management is played by Risk Division, which operates as a permanent organizational structure, with roles and responsibilities related to the administration of the general framework of risk management and also Finance and Planning / Financial Management Division. These Divisions offer support to the Risk Management Committees and to the management of the Bank through the continuous monitoring of the risks related to the Bank activity.

**UniCredit Consumer Financing**

The Supervisory Board is responsible for the set up and keeping of a proper and effective internal control system.

The Management Board is responsible for implementing the strategy and the policies on risk management as established and defined in the Article of Association and the Internal Governance Rules.

For the support of the risk management activities, specialised committees are set-up within the financial institution: Audit Committee, Risk Management Committee and Credit Committee.

Risk and Collection Division operates as a permanent organizational structure, with responsibilities related to the administration of the general framework of risk management. The Risk Division offers support to the Risk Management Committee and the company's management through the current monitoring of the credit risk.

The Finance and Planning Division offers support to the Risk Management Committee and the company's management through the current monitoring of the market and liquidity risk.

Marketing and Product Development Department offers support to Risk Management Committee and the company's management through the current monitoring of the reputation risk.

Operational risk is managed by all the departments whose activities incur operational risks.

The monitoring is ensured by operational risk function by regular verification of the limits of operational risk indicators.

Risk management function is supported at company level by other specialized committees (Discipline Committee, Norms and Procedures Committee, Projects Committee, Product and Pricing Committee, Business Continuity and Crisis Management Committee, etc.).

**UniCredit Leasing Corporation**

Organizational structures responsible for risk management:

The Supervisory Board is responsible for the set up and keeping of a proper and effective internal control system.

The Board of Directors is responsible for implementing the strategy and the policies on risk management.

Risk Management Committee - is a strategic committee and has the responsibility of identification, evaluation and management of significant risks and has to meet at least quarterly or any time when required.

Audit Committee is responsible to assist the Company's Board in defining and preparing the principles and guidelines governing the entity's entire internal control system, on the basis of a risk-oriented approach, and assessing its effectiveness and efficiency, so that the main risks are properly identified, then measured, managed and monitored, subject to the Board's responsibility for all decisions on this matter..

Credit Committee has responsibilities of approval of the new transactions and credit reviews as per competences framework in order to assure the required quality of the portfolio and to limit the credit risk as required by the credit policies.

The Special Credit Committee is responsible for approval of restructured cases, IFRS provisioning level for individually assessed clients, according to competencies and specific Regulation.

Permanent Workgroup Committee for Operational Risks is responsible for operational risk identification, mitigation actions proposed and monitoring of the mitigation actions in place.

Credit Operations Division functions as a permanent organizational structure, with responsibilities related to management of general framework for risk management and supports Risk Management Committee and the Board of Directors by ensuring the monitoring systems for the management of significant risks.

UniCredit Bank

## 2. Scope of application

### 2.1. Relevant scope of consolidation

The Report is prepared in accordance with National Bank of Romania Regulation no. 5/2013 regarding prudential requirements for credit institutions and Regulation no. 575/2013 of European Parliament and Council dated 26.06.2013 regarding prudential requirements for credit institution and investment companies and amending Regulation (UE) no.648/2012 in order to detail the information published in the Annual Report 2016. The documents are available in electronic format at www.unicredit.ro.

The institution subject to disclosure is **UniCredit Bank SA.** ("the Bank"), the report includes Bank information and also information regarding the entities integrated in the consolidated prudential area of UniCredit Bank.

Starting with August 2016, UniCredit Bank S.A. (the "Bank") is the new brand name of formerly UniCredit Tiriac Bank SA that was established as a Romanian commercial bank on 1 June 2007 upon the merger by acquisition of the former UniCredit Romania S.A. (the absorbed bank) by Banca Comerciala HVB Tiriac S.A. (the absorbing bank) and is licensed by the National Bank of Romania ("NBR") to conduct banking activities.

The Bank's current registered office is 1F, Expozitiei Boulevard, District 1, Bucharest, Romania.

UniCredit Bank S.A. is controlled by UniCredit SpA (Italy), with registered office in Rome, Italy, Via Alessandro Specchi,16.

The Bank provides retail and commercial banking services in Romanian Lei ("RON") and foreign currency for individuals and legal entities. These include: accounts opening, domestic and international payments, foreign exchange transactions, working capital finance, medium and long term facilities, retail loans, bank guarantees, letter of credits and documentary collections, derivative financial instruments.

UniCredit Bank Group is exercising direct and indirect control over the following subsidiaries:

- UniCredit Consumer Financing IFN S.A., having its current registered office at 23-25 Ghetarilor street, 1st and 3rd floor, District 1, Bucharest, Romania, provides consumer finance loans to individual clients. The Bank has a shareholding of 50.1% in UCFIN since January 2013.

- UniCredit Leasing Corporation IFN S.A.("UCLC"), having its current registered office at 23-25 Ghetarilor Street, 1st, 2nd and 4th floor, District 1, Bucharest, Romania, provides financial lease services to corporate clients and individuals. UCLC, previously associate entity, has become a subsidiary of the Bank starting with April 2014 when the Bank obtained 99.95% direct and indirect controlling interest (direct controlling interest: 99.90%). The Bank's shareholding has changed to an indirect controlling interest 99.98% as of 31 December 2016 (direct controlling interest: 99.96%), as a result of the merger of UCLC with UniCredit Leasing Romania SA ("UCLRO") finalized by June 2015, where UCLRO was absorbed by UCLC.

- Debo Leasing IFN S.A., having its current registered office in 23-25 Ghetarilor Street, 2nd floor, 1st district, Bucharest, Romania, is a real estate finance lease entity, in which the Bank has an indirect controlling interest of 99.97% (31 December 2015: 99.97%) through UCLC.
- UniCredit Insurance Broker S.R.L., having its current registered office in 23-25 Ghetarilor Street, 2nd floor, 1st district, Bucharest, Romania, intermediates insurance policies related to leasing activities to legal entities and individuals, in which the Bank has an indirect controlling interest of 99.98% (31 December 2015: 99.98%) through UCLC.

The Report presents information at consolidated level and, as specified, information for UniCredit Bank Group's entities at individual level.

### *2.2. Entities deducted from Own Funds*

According to Regulation no. 575/2013 of European Parliament and Council dated 26.06.2013 regarding prudential requirements for credit institutions and investment companies, the holdings in Common Equity Tier 1 (CET1) that are classified as significant investments shoud be deducted from own funds if the CET1-threshold for deduction is exceeded.

As at 31 December 2016, UniCredit Bank holds at individual level significant investments in financial entities which were not deducted from own funds as the CET1-threshold was not exceeded.

### *2.3. Entities added to RWA*

As at 31 December 2016, the significant investments in financial entities are shown at the individual level with a risk weight of 100% as they are not deducted from own funds, but are included in the consolidated perimeter.

### *2.4. Description of the UniCredit Group composition in Romania and consolidation methodology*

The management of the entities in the UniCredit Group is governed by a two-tier system, by the Management Board and respectively by the Supervisory Board, in accordance with the prerogatives provided by the Constitutive Deed and within the authority levels given by the General Assembly of Shareholders. The members of the Management Board exercise their responsibilities under the oversight of the Supervisory Board.

UniCredit Bank

**UniCredit Bank**

Number of mandates held by members of management structure of UniCredit Bank S.A.:

| MB Members | Mandates in MB / Board of Directors of UCB | Mandates in SB / Supervisory Board of UCLC | Mandates in SB / Supervisory Board of UCFIN |
|---|---|---|---|
| Catalin Rasvan Radu - Executive President | Four | Four | Four |
| Marco Cravario - First Executive Vice-president | First | First | First |
| Daniela Margareta Bodirca - Executive Vice-president | Three | Four | Two |
| Alina Dragan - Executive Vice-president | Two | - | - |
| Marco Giuseppe Esposito - Executive Vice-president | Two | - | - |
| Mihaela Alina Lupu - Executive Vice-president | Two | Two | - |
| Jakub Dusilek Executive Vice-president | First | First | - |

**Policy regarding the selection and appointment of board members**

The Nomination Committee (CN) is a permanent committee established by the Supervisory Board of UniCredit Bank. It is responsible, among others, to identify and recommend to the Supervisory/Management Board, for approval, candidates to occupy the vacant seats within the management body and to assess the balance of knowledge, skills, diversity and experience within the management body.

Once the Nomination Committee has identified a candidate for Supervisory/Management Board position, it assesses the respective candidate according to a "Fit & Proper" internal procedure (Rules for the selection and assessment of Management Board and Supervisory Board members and for assessing the suitability of key function holders) based on at least the following documents: Curriculum Vitae, information about job- specific expertise, personal reliability and good repute, extract from criminal records, and two governance criteria: information about availability (time resources) and information about relations to the credit institution.

This assessment is done once a year for every member of the Management Body (Management Board and Supervisory Board).

At the end of 2016 the Nomination Committee had 3 members.

**The Policy regarding Diversity in the Selection of People in the Management Structures**

As of the year end of 2016, there were 4 women in the management of UniCredit Bank (3 out of 7 members of Management Board and 1 out of 7 members of Supervisory Board).

The Group Policy on the structure, composition and remuneration of the Corporate Bodies of Group Companies states that, for the purpose of increasing the number of women on the Corporate Bodies of leading Group Companies and with the aim of reaching at least one third of the members of the Management Board (Supervisory Board and Management Board), the Parent Company has adopted the promotion of women to Corporate Bodies as best practice within the Group.

To that end, a proposal was approved by the Nomination Committee and by the Supervisory Board and by the Management Board in order to approve the 1/3 target of women in the composition of the management body, within a time horizon of 31.12.2016.

At the end of 2016 there were 4 women in the Management Body of UniCredit Bank (3 out of 7 members in Management Board and 1 out of 7 members in Supervisory Board).

When an external provider is involved in the recruitment process the Bank assures that they know about the commitment in implementing the agreed targets and follow the global policy regarding gender equality.

## *2.5. Substantial or legal impediments that hinder the rapid transfer of capital resources within the Group*

At UniCredit Group level, an integrated analysis is done to identify the significant risks. The processes for management, monitoring and reporting of risks are formalized in the Group regulations, aligned and integrated at the local group at UniCredit Bank SA level. In accordance with the rules regarding the analysis process, calibration, approval, adoption, implementation, monitoring and reporting of the Group regulations, UniCredit Bank SA has the responsibilitaty of transmiting of the applicable regulation to its subsidiaries, in order to be analized, approved/adopted and implemented. Subsequently, UniCredit Bank SA assesses and decides the aplicability at its subsidiaries level taking into account the nature, dimension and complexity of the their activities.

UniCredit Bank

In order to ensure the control over implementation of the Group requirements at level of direct controlled entities, there is a frequent reporting process regarding the status of local implementation under the Internal Control Committee of UniCredit Bank SA.

The main potential impediments regarding the rapid transfer of capital resources are addressed below:

**2.5.1. The impact of legal status of subsidiaries regarding the prompt transfer of funds and/or debt reimbursement.**

*UniCredit Consumer Finance IFN SA*

UniCredit Bank SA (UCB) controls UniCredit Consumer Financing (UCFin) through majority of voting rights held (50.1%), which implies the approval of development plan and strategy of UCFIN in accordance with Bank and UniCredit Group's strategy.

The control exercised over UCFIN is strengthen of the fact the UCB appoints 4 out of 5 members of UCFIN Supervisory Board in accordance with UCFIN Articles of Association („AoA" or Constitutive Act). In Accordance with AoA, the UCFIN Supervisory Board has the authority to check the Board Member's activity in respect of the implementation of the Bank's strategy, aligned with those of UniCredit Group.

As a result, there is no impediment which could adversely impact the prompt transfer of funds from UCFIN to UCB and/or the UCFIN capacity for fast reimbursement of debts to UCB.

*UniCredit Leasing Corporation IFN SA*

UniCredit Bank SA (UCB) controls UniCredit Leasing Corporation IFN S.A. (UCLC) through majority of voting rights held (99.98%), which implies the approval of development plan and strategy of UCLC in accordance with Bank and UniCredit Group's strategy.

The control exercised over UCLC is strengthen of the fact the UCB appoints all 5 members of UCLC Supervisory Board in accordance with UCLC Articles of Association („AoA" or Constitutive Act). In Accordance with AoA, the UCLC Supervisory Board has the authority to check the Board Member's activity in respect of the implementation of the Bank's strategy, aligned with those of UniCredit Group.

As a result, there is no impediment which could adversely impact the prompt transfer of funds from UCLC to UCB and/or the UCLC capacity for fast reimbursement of debts to UCB.

The Articles of Associations of UCFIN and UCLC do no include limitations, restrictions regarding the transfer of own funds and/or debt reimbursement.

**2.5.2. Assessment of the other interests, different from those (controlling interests) of UCB and of their impact. UCB capacity to ask for the funds transfers or debt reimbursements.**

No other interests were identified except the UCB controlling interests as the control is defined in the Articles of Associations of the 2 subsidiaries.

Meanwhile, we mention that the financing agreements concluded between UCB and their subsidiaries contain contractual clauses regarding the situations where repayments in advance can appear and where collateral guarantees are in place, where all actual and future cash amounts are pledged in the bank's favour. (credit balances in the bank accounts open at UCB).

**2.5.3. Potential unfavorable fiscal impact for UCB or its subsidiaries in case of funds transfer or debt reimbursement**

At UniCredit Bank SA level there is no adverse fiscal impact as a result of the potential prompt transfer of funds or debt repayment in advance in accordance with the Fiscal Code provisions in force starting with 1st of January 2016.

At subsidiaries level, in hypothethical case of capital distribution, there is no effect that could generate a fiscal impact.

**2.5.4. Eventual prejudices could result from the business strategies of subsidiaries regarding the prompt transfer of funds and/or debt reimbursement**

2017 budget and financial plan for next 3 years of UCB and its subsidiaries outline the intention of ongoing business activity and to support for the implementation of the subsidiaries strategies. In normal conditions of ongoing business activity, there has not been forecasted any prompt transfer of funds and/or debt repayments in advance in the financial plans.

**2.5.5. Analysis of the impact of contractual relationships betwee the subsidiaries and UCB/other third parties regarding the prompt transfer of funds and/or debts repayment.**

The contractual relationships between UCB and its subsidiaries are approved and monitored in accordance with the provisions of Articles of Association of subsidiaries and internal procedures which regulates the competencies levels for approval set up by managements and their shareholders.

Taking into account the shareholders structure, there is no negative risk that could impact the contractual business relationships of subsidiaries.

**2.5.6. The historical and forecast flows of funds between UCB and its subsidiaries with potential impact on capacity of prompt transfer of funds and/or debt reimbursement**

The loan agreements concluded by UniCredit Bank and its subsidiaries includ the calculation of penalty interest in case the loans' payments obligations are not met. The penalty interest is applied at the maturity date, until the full payment date and it is applied to outstanding amount. There has no been cases in the past for the penalty interest to be applied for the credit lines granted to subsidiaries of UCB.

Meanwhile, we have to mention that, in accordance with the provisions of article 26 of NBR Regulation no.5/2013, UCB, as parent credit institution, takes into account and balance the interests of its subsidiaries and analyzes them continuously in the way those interests contributes to the objectives and interests of UCB Group and respectively of UniCredit Group, taken together as one objective/interest, on a long term basis.

**2.5.7. Intragroup Liquidity Transfers**

Intra-group liquidity transfers are subject to restrictions due to legal and regulatory constraints.

With reference to regulatory requirements, it should be noted that UniCredit Bank is subject to rules provided by The Regulation (EU) No 575/2013 on "prudential requirements for credit institutions and investment firms".

# 3. Own funds

## *3.1. Regulatory capital - summary reconciliation and changes over time*

Starting with January 2014, Romanian Banking System is applying the Basel III norms, in accordance with Regulation no. 575/2013 of European Parliament and Council dated 26.06.2013 regarding prudential requirements for credit institutions and investment companies and amended by Regulation (UE) no.648 / 2012 and by Regulation no. 5/2013 regarding prudential requirements for credit institutions issued by National Bank of Romania.

The prudential requirements define the eligibility criteria for capital instruments which shall be included in Own Funds – Common Equity Tier 1 Capital, Additional Tier 1 Capital or Own Funds – Tier 2 Capital.

The composition of the equity for the regulatory purpose is detailed by the own funds report of the Bank at 31.12.2016, as detailed below:

*-RON-*

UniCredit Bank

| Own Funds – consolidated view | 31-Dec-16 | 31-Dec-15 | (%) |
|---|---|---|---|
| **OWN FUNDS** | **3,128,289,473** | **2,982,319,884.00** | **4.89%** |
| **TIER 1 CAPITAL** | **2,924,262,263** | **2,788,504,898.00** | **4.87%** |
| **COMMON EQUITY TIER 1 CAPITAL*** | **2,924,262,263** | **2,788,504,898.00** | **4.87%** |
| Capital instruments eligible as Common Equity Tier 1 capital | 1,101,604,121 | 1,101,604,121.00 | **0.00%** |
| Retained earnings*** | 1,745,759,399 | 1,604,683,016.00 | **8.79%** |
| Accumulated other comprehensive income | -3,349,870 | 45,007,535.00 | **-107.44%** |
| Other reserves | 178,426,959 | 176,548,582.00 | **1.06%** |
| Funds for general banking risk | 51,453,474 | 38,431,254.00 | **33.88%** |
| Minority interest given recognition in Common Equity Tier 1 capital | 43,086,036 | 54,183,634.00 | **-20.48%** |
| Adjustments to Common Equity Tier 1 due to prudential filters | 49,382,872 | 42,228,229.00 | **16.94%** |
| (-) Other intangible assets | -153,301,164 | -153,342,560.00 | **-0.03%** |
| (-) IRB shortfall of credit risk adjustments to expected losses | -81,080,701 | -85,410,878.00 | **-5.07%** |
| (-) Excess of deduction from Additional Tier 1 items over Additional Tier 1 Capital | -78,537,711 | -117,793,410.00 | **-33.33%** |
| Other transitional adjustments to Common Equity Tier 1 Capital | 70,818,848 | 82,365,375.00 | **-14.02%** |
| **ADDITIONAL TIER 1 CAPITAL** | **0.00** | **0.00** | **n/a** |
| Other transitional adjustments to Additional Tier 1 Capital | -78,537,711 | -117,793,410.00 | **-33.33%** |
| Excess of deduction from Additional Tier 1 items over Additional Tier 1 Capital (deducted in Common Equity Tier 1) | 78,537,711 | 117,793,410.00 | **-33.33%** |
| **TIER 2 CAPITAL 2**** | **204,027,210** | **193,814,986.00** | **5.27%** |
| Paid up capital instruments and subordinated loans | 220,243,350 | 219,438,250.00 | **0.37%** |
| Other transitional adjustments to Tier 2 Capital | -16,216,140 | -25,623,264.00 | **-36.71%** |

| | | | |
|---|---|---|---|
| **Total Capital Ratio** | **12.43%** | **13.13%** | **-5.34%** |

UniCredit Bank

*** Capital instruments qualify as equity instruments Level 1 basic eligibility if the conditions listed below are fulfilled:**

- *Instruments are issued directly by the institution with the prior approval of shareholders institution or, where permitted under applicable national legislation governing body of the institution;*
- *Instruments are paid, and their purchase is not funded directly or indirectly by the institution; are classified as equity within the meaning of applicable accounting framework;*
- *Instruments are presented clearly and distinctly in the balance sheet in the financial statements of the institution;*
- *Instruments are perpetual*
- *The instruments meet the following conditions in terms of distributions:*

  - *No preferential treatment in terms of distribution order to perform distributions, including in relation to other instruments Tier 1 instruments and the conditions governing the instruments do not provide preferential rights to making distributions;*
  - *Distributions to holders of the instruments may be made only items that can be distributed;*
  - *The conditions governing the instruments do not include a cap or other restriction on the maximum level of distributions;*
  - *The level of distributions is not determined based on the purchase price of the instruments at issue.*

- *The conditions governing the instruments do not include any obligation for the institution to make distributions to their owners, and the institution is not otherwise subject to such obligations;*

  - *Failure distributions is not an event of default for the institution;*
  - *Annual distributions do not impose restrictions on the institution.*

**** Capital instruments qualify as equity instruments Level 2 if the conditions for eligibility listed below are fulfilled:**

- *Subordinated loans are obtained and fully paid;*
- *Subordinated loans are not issued by a subsidiary or an associate;*
- *Providing subordinated loans is not funded directly or indirectly by the institution; the principal debt subordinated loans under the provisions governing subordinated loans, is entirely subordinated to the claims of all unsubordinated creditors;*
- *Subordinated loans have an original maturity of at least five years;*
- *Provisions governing, subordinated loans do not include any incentive for their principal amount to be refunded or, if applicable, returned by the institution before maturity;*
- *Subordinated loans can be recognized in the category of Tier 2 items if in the opinion of the National Bank of Romania meet the eligibility conditions listed above.*

**** In accordance with the Regulation 575/2013, the net profit of the year is not included in the calculation of total own funds until its distribution is not approved by GSM, for comparability reasons in both years.*

# 4. Capital requirements

## 4.1. *General comment*

**Capital Adequacy Assessment**

During 2016, within the Bank it was continued the sustained process for completing the internal methodological framework with specific regulations, mainly as regards to ICAAP general framework, stress tests, setting and monitoring of risk appetite, capital management rules, rules regarding the new risks identified by the Bank as significant.

The Internal Capital Adequacy Assessment Process ("ICAAP") was performed in accordance with National Bank of Romania Regulation no 5/2013, with subsequent amendments and modifications, representing an independent assessment of the current and future internal capital, related to the risks the bank is facing and in line with the Bank's strategy. That is to say that UCB assesses the balance between the assumed risk and the available capital consistently with the strategy and assumed objectives, respectively the internal capital and the available financial resources.

The internal capital is represented by the sum of the economic capitals calculated for each risk: credit risk, market risk, operational risk, business risk, financial investments risk, real estate investments risk based on internal models (ex. CVaR, VaR etc).

The ultimate mission of the capital adequacy is to ensure that it forms an integral part of day-to-day management and decision-making processes such as: embedding risk management measures and the capital needed in strategic planning, introduction of risk analysis in strategic planning and budgetary processes.

Thus, the Bank develops and manages its risk management processes, respectively implements processes and tools to assess the level of internal capital adequate to support each type of risk, including those risks not captured by the total capital requirement (i.e. Pillar I risks), within the scope of an assessment of the Bank's Legal current and future exposure, taking account its strategies and developments in its business environment.

**Necessary regulated own funds at consolidated level**

For calculating the regulatory capital requirements for credit risk, the Bank applies the Foundation Internal Rating Based Approach, according to Regulation no. 575/2013 of European Parliament and Council dated 26.06.2013 regarding prudential requirements for credit institutions and investment companies and amending Regulation (UE) no. 648/2012 of the Comission for establishing technical standards for reporting for supervisory purposes and by Regulation no. 5/2013 regarding prudential requirements for credit institutions issued by National Bank of Romania (due to the joint approval received from Bank of Italy, FMA and National Bank of Romania) for the following segments of clients: corporate (except for real estate clients and specialized financing), multinational companies, banks, sovereigns and central banks and securities industries. For the rest of the portfolio, the Bank continued to use the standardized approach.

For calculating the regulatory capital requirements for market risk, the Bank used the Standardised Approach, while, for operational risk, it is used advanced approach in accordance the above mentioned regulations. All tasks related to the calculation and monitoring of capital requirements are performed by specialized units of Finance Division and Risk Division of the Bank.

For complying with capital adequacy requirements established by Emergency Ordinance 99/2006, the Bank is actively involved in an evaluation process of capital requirements, for sustaining current and future activity, which implies the following processes:

- Bugeting
- Monitoring and analysis
- Stress testing
- Forecasting

**Quantitative Information**

*- RON –*

| OWN FUNDS REQUIREMENTS – consolidated view | 31-Dec-16 | 31-Dec-15 | (%) |
|---|---|---|---|
| **TOTAL RISK EXPOSURE AMOUNT** | **25,168,313,279** | **22,709,793,253** | **10.83%** |
| **RISK WEIGHTED EXPOSURE AMOUNTS FOR CREDIT, COUNTERPARTY CREDIT AND DILUTION RISKS AND FREE DELIVERIES** | **22,815,934,194** | **20,361,212,845** | **12.06%** |
| ***Standardised Approach (SA)*** | ***10,167,891,375*** | ***9,103,169,549*** | **11.70%** |
| **SA exposure classes excluding securitization positions** | **10,167,891,375** | **9,103,169,549** | **11.70%** |
| Central governments or central banks | 97,172,254 | - | **n/a** |
| Regional governments or local authorities | 204,371,509 | 223,138,898 | **-8.41%** |
| Public Sector Entities | - | 13,235 | **n/a** |
| Institutions | 110,136,265 | 146,493,065 | **-24.82%** |
| Corporate | 2,912,043,608 | 2,595,584,756 | **12.19%** |
| Retail | 3,212,941,618 | 2,780,669,368 | **15.55%** |
| Exposures secured by mortgage of immovable property | 1,456,331,270 | 1,084,370,851 | **34.30%** |
| Exposures in default | 1,578,959,855 | 1,653,022,845 | **-4.48%** |
| Items associated with particularly high risk | 56,328,978 | 125,479,193 | **-55.11%** |
| Claims on institutions and corporates with a short-term credit assessment | 9,093,352 | 6,800 | **n/a** |
| Equity | 5,029,257 | 5,029,294 | **0.00%** |

| | | | |
|---|---|---|---|
| Other elements | 525,483,409 | 489,361,244 | **7.38%** |
| ***Internal Ratings Based Approach (IRB)*** | ***12,648,042,819*** | ***11,258,043,296*** | **12.35%** |
| **IRB Approach where neither own estimates of LGD nor Conversion Factors are used** | **12,591,613,147** | **11,090,707,592** | **13.53%** |
| Central governments or central banks | 432,691,777 | 460,039,175 | **-5.94%** |
| Institutions | 829,597,665 | 691,597,434 | **19.95%** |
| Corporate - SME | 5,845,914,472 | 5,223,348,927 | **11.92%** |
| Corporate - Other | 5,483,409,233 | 4,715,722,056 | **16.28%** |
| **Equity IRB*** | **56,429,672** | **167,335,704** | **-66.28%** |
| **TOTAL RISK EXPOSURE AMOUNT FOR POSITION, FOREIGN EXCHANGE AND COMMODITIES RISKS** | **183,998,793** | **94,930,417** | **93.82%** |
| **TOTAL RISK EXPOSURE AMOUNT FOR OPERATIONAL RISK** | **2,165,692,698** | **2,250,661,491** | **-3.78%** |
| **TOTAL RISK EXPOSURE AMOUNT FOR CREDIT VALUATION ADJUSTMENT** | **2,687,594** | **2,988,500** | **-10.07%** |

*Please refer for more details below at point 4.3.

### *4.2. Capital Strengthening*

From the bank's perspective, Tier 1 capital is the core measure of its financial health and is assessed from the view of its capacity to absorb losses without ceasing business operations. Under Basel III, the minimum tier 1 capital ratio is 6%, which is calculated by dividing the bank's tier 1 capital by its total risk-weighed assets.

As at December 2016, the bank did not hold additional Tier 1 instruments, therefore Core Tier 1 ratio was calculated at the level of tier 1 ratio, with a consolidated level of 11.62%, significantly higher than the minimum regulatiory requirement.

### *4.3. Reclassification of financial assets table*

As at December 2016, Visa Inc (USA) preferred shares series C (resulting from the VISA Europe Ltd acquisition by VISA Inc) were initialy recognized as equity investment available for sale at fair value.
The fair value of VISA Inc share have been estimated based on the methodology and approach developed by parent company UniCredit SpA and distributed within the UniCredit Group to all it subsidiaries.

### *4.4. Risk Management and business model - RWA segmentation*

One of the Bank's strategic objectives was the development of a sound risk culture extended both at management level and at the level of all business units with risk management responsibilities, by determining firm-wide views on acceptable relationships between the risks and profitability at a Bank's overall level and for each significant activity in order to ensure sustainability of sound and prudent operations.

UniCredit Bank targeted a balanced asset in order to diminish the exposures that have a high risk associated. Also, the bank performed processes for RWA optimization.

### *4.5. RWAs and business activities*

According to Basel III framework, the total RWA are the sum of:

- RWA Credit Risk (RWA Banking book+RWA Counterparty Risk+ RWA Securitisation)
- RWA equivalent Market Risk
- RWA equivalent Operational Risk

### *4.6. Capital surcharges & buffers*

Regulation no. 5/2013 issued by National Bank of Romania includes specific provisions for capital buffers that may be applicable on top of minimum capital requirements. The following buffers were imposed by the National Bank of Romania through Order no 11/2015 and Order no 12/ 2015:

| New capital requirements | 2016 |
|---|---|
| Capital conservation buffer (affecting CET1) | 0.625% |
| Countercyclical capital buffer (affecting CET1) | 0% |
| O-SII buffer (affecting CET1) | 1% |

Additionally, College of Supervisors of European Central Bank (ECB), in line with the local Supervisory Review and Evaluation Process (SREP) assessment carried out by the National Bank of Romania, decided that UniCredit Bank S.A. shall maintain a solvency ratio above 10%.

### *4.7. Capital planning- targeted level of capital*

As per Regulation 575/ 2013, the Minimum Capital Requirement is set to 8% of Risk Weighted Assets.

Based on common decision European Central Bank and National Ba nk of Romania, UniCredit Bank must at all times satisfy the total capital ratio (solvency ratio) of 10%.

### *4.8. RWA calculation method and models*

The bank calcules RWA according to the stipulations of Regulation EU no 575/2013 of the European Parliament and of the Council, using the following approaches:

**Standardized Approach:**

Risk-weighted exposure amount is calculated by using Fixed Regulatory Risk Weights (RW) and depends on the obligor type (Corporate/ Retail) and external rating (if available)

**Internal Rating Base (IRB) Approach:**

Risk-weighted exposure is calculated by using Calculated Risk Weights (RW) based on internally built credit risk parameters: Probability of default (PD), Loss given default (LGD), Exposure at default (EAD), M (Maturity).

In **Internal Rating Base** approach, Capital Reserve is adequate to the specific risk profile of the portfolio.

### *4.9. RWA changes overtime*

In July 2012, the Bank has obtained the joint approval of Bank of Italy, Financial Market Authority and National Bank of Romania to use the Foundation – Internal Rating Based approach for the calculation of minimum capital requirements for the following client segments: corporate clients (except for real estate clients and specialized financing), multinational companies, banks, sovereigns and central bank and securities industries clients.

Further, for the rest of the portfolio, the Bank continued to apply the Standardized approach.

## 5. Credit risk

### *5.1. Risk Management organization*

**Strategies, policies and processes for credit risk management**

Credit risk strategy is established by all the Bank's activities that present a significant exposure to credit risk. The Bank's credit risk strategy is reviewed periodically, at least once a year, and is approved by the Bank's management structure. The credit risk strategy reflects the tolerance to risk and the profitability level which the Bank intends to achieve in the conditions of the exposure to the assumed risks.

The Bank has established risk management processes and has tools in order to identify, measure, monitor and control the credit risk.

The Bank's credit risk management policy promotes a set of coherent principles and practices, oriented towards the following main directions:

- Establishment of a framework and adequate parameters of credit risk;
- Promotion and operation of a healthy and solid credit granting process;

- Promotion and maintenance of an adequate process for credit administration, measurement and monitoring;
- Permanent control over the quality of the loan portfolio.

The credit risk management is performed taking into consideration the credits both at individual level and at whole portfolio level and includes the consideration of the qualitative and quantitative aspects related to risks.

Credit risk management is realised by limiting credit risk exposures setting limits established in accordance with general strategy of the Bank (limits established by sectors of activity, zones / geographical areas, counterparty categories, type of products, residence, country and currency, etc.)

These limits are monitored and periodically reported to relevant committees.

Credit risk management processes within UniCredit Bank imply the following:

- Acurate definition of specific processes and procedures for credit risk management differentiated depending on the main components of credit risk and the stage of the credit granting process, as follows:
  - Procedures of risk management at credit granting stage;
  - Procedures to prevent and mitigate default risk, settlement risk, concentration risk and residual risk;
  - Procedures for the prevention and mitigation of the risk related to foreign currency lending for debtors exposed to currency risk;
  - Specific procedures for identification and management of „problem" assets.
- Adequacy of credit risk procedures, policies and management tools, in line with the strategy:
  - Identification of the risk associated to the customer by applying internal rating specific for each client category; the analysis of the customer's rating, which is achieved by an internal assessment system;
  - Requesting complete and adequate proving documents from customers according to the type of financing and to the associated risk;
  - Approval of the standard parameters of lending products by taking into account the analysis of the associated risks;
  - Continuous monitoring of the loan portfolio;
- Exposure collateralization with eligible collaterals according to the legal stipulations in force, and also based on the Basel III implementation approach and relevant internal norms and procedures;
- Other credit risk mitigation techniques.

The credit risk management process is considering the appropriate allocation of duties that are clearly defined in specific lending procedures so as not to be assigned responsibilities that lead to conflicts of interest.

**The scope and type of reporting and measuring systems for credit risk**

UniCredit Bank

In order to evaluate the basis of prudential exposure to credit risk, in the Bank implemented rating systems (through consideration of quantitative factors, qualitative factors and payment behavior related factors), for all categories of clients in order to realise the classification of exposures based on the assessment borrowers' credit risk throughout the entire loan life cycle, by reference to a general scale assessment of default risk.

In UniCredit Bank internal ratings and default probability plays an essential role in the entire process of credit risk management. Rating assessment is an important part of the credit approval process. Credit risk tolerance is considering limits for granting credit exposures on rating classesDuring the credit life cycle, the rating information is an important part of monitoring as well as of restructuring and of the progress of the problem credits.

In addition, the risk reporting and portfolio management focuses on rating (in addition to information on debt service).

### *5.2. Assets & Liabilities by Residential Contractual Maturity*

Assets & Liabilities by Residual Contractual Maturity, consolidated view:

\- *RON* -

| 31 December 2016 | Up to 3 months | 3 months to 1 Year | 1 Year to 5 Years | Over 5 Years | No fixed maturity | Total contractual amount | Total carrying amount |
|---|---|---|---|---|---|---|---|
| Cash and cash equivalents | 5,806,429,168 | - | - | - | - | 5,806,429,168 | 5,806,429,168 |
| Financial assets at fair value through profit or loss | 393,119,265 | - | - | - | - | 393,119,265 | 393,119,265 |
| Derivatives assets designated as hedging instruments | 17,325,503 | - | - | - | - | 17,325,503 | 17,325,503 |
| Fair value changes of the hedged items in portfolio hedge | 26,783 | - | - | - | - | 26,783 | 26,783 |
| Loans and advances to banks | 213,669,687 | 102,073,745 | 422,038,867 | - | - | 737,782,299 | 737,782,299 |
| Loans and advances to customers | 3,364,001,881 | 6,790,585,386 | 5,986,730,929 | 4,503,934,938 | - | 20,645,253,134 | 20,476,755,183 |
| Net Lease receivables | 523,603,708 | 891,753,545 | 1,550,780,132 | 191,547,168 | - | 3,157,684,553 | 3,157,684,553 |
| Investment securities, available for sale | 209,099,030 | 893,514,457 | 3,051,248,205 | 2,197,311,406 | 20,280,520 | 6,371,453,618 | 6,371,453,618 |
| Total other financial assets, net value | 65,615,181 | - | - | - | - | 65,615,181 | 65,615,181 |
| **Total financial assets** | **10,592,890,206** | **8,677,927,133** | **11,010,798,133** | **6,892,793,512** | **20,280,520** | **37,194,689,504** | **37,026,191,553** |
| Derivative liabilities at fair value through profit or loss | 99,316,461 | - | - | - | - | 99,316,461 | 99,316,461 |
| Derivatives liabilities designated as hedging instruments | 98,730,581 | - | - | - | - | 98,730,581 | 98,730,581 |
| Deposits from banks | 2,474,043,192 | 699,352,822 | - | - | - | 3,173,396,014 | 3,173,396,014 |
| Loans from banks and subordinated liabilities | 1,916,007,497 | 2,656,949,965 | 2,650,332,799 | 535,787,155 | - | 7,759,077,416 | 7,756,728,895 |
| Deposits from customers | 20,689,738,820 | 1,114,301,434 | 168,720,339 | 22,838,223 | - | 21,995,598,816 | 21,995,286,812 |
| Debt securities issued | - | 1,626,644 | 550,000,000 | - | - | 551,626,644 | 551,024,752 |
| Total other financial liabilities | 227,160,438 | | | | | 227,160,438 | 227,160,438 |
| **Total financial liabilities** | **25,504,996,989** | **4,472,230,865** | **3,369,053,138** | **558,625,378** | **-** | **33,904,906,371** | **33,901,643,953** |
| | | | | | | | |
| **Liquidity surplus/ (shortfall)** | **-14,912,106,783** | **4,205,696,268** | **7,641,744,995** | **6,334,168,134** | **20,280,520** | **3,289,783,134** | **3,124,547,601** |
| Adjustment for investment securities available for refinancing * | 6,142,074,068 | -893,514,457 | -3,051,248,205 | -2,197,311,406 | - | - | - |
| **Liquidity surplus/ (shortfall) adjusted** | **-8,770,032,715** | **3,312,181,811** | **4,590,496,790** | **4,136,856,728** | **20,280,520** | **3,289,783,134** | **3,124,547,601** |

### 5.3. *Credit risk profile and concentrations*

**Credit risk - Quantitative Information**

**Geographical distribution of exposures (including securities issued by the Ministry of Public Finance), distributed by main classes of exposures:UniCredit Bank – *individual view***

*- RON -*

| Geographic Area | 31.12.2016 | | | | | | |
|---|---|---|---|---|---|---|---|
| | STANDARDIZED APPROACH | | | | INTERNAL RATING MODELS BASED APPROACH | | |
| | Companies | Retail | Institutions | Central administration or central banks | Central administration or central banks | Companies | Institutions |
| Banat | 204,781,892 | 333,288,630 | | | | 698,539,431 | 837,780 |
| Bucharest | 1,478,769,801 | 2,448,924,204 | 70,922 | 9,937,893,549 | 986,381,021 | 4,450,439,060 | 1,416,057,353 |
| Crisana-Maramures | 186,264,353 | 178,329,555 | | | | 626,593,569 | 12,501,571 |
| Dobrogea | 177,859,739 | 350,189,402 | | | | 452,711,152 | |
| Moldova | 1,383,107,779 | 568,009,213 | | | | 1,165,784,987 | 496,680 |
| Muntenia | 183,727,962 | 187,755,763 | | | | 918,580,240 | 274,164 |
| Oltenia | 237,232,389 | 332,368,667 | | | | 929,640,561 | 705,493 |
| Transilvania | 534,603,045 | 506,759,684 | | | | 1,498,359,861 | 404,237 |
| *TOTAL* | **4,386,346,960** | **4,905,625,117** | **70,922** | **9,937,893,549** | **986,381,021** | **10,740,648,862** | **1,431,277,280** |

**UniCredit Consumer Financing –*individual view***

*- RON -*

| Geographic Area | 31.12.2016 | | |
|---|---|---|---|
| | STANDARDIZED APPROACH | | |
| | Companies | Retail | Central administration or central banks |
| South | - | 332,889,099 | - |
| Nord | - | 257,191,355 | - |
| East | - | 432,774,030 | - |
| Bucharest | - | 737,821,909 | - |
| TOTAL | - | **1,760,676,393** | - |

UniCredit Bank

## Leasing Companies – *sub-consolidated view*

- *RON* –

| Geographic Area | 31.12.2016 | | |
|---|---|---|---|
| | STANDARD APPROACH | | |
| | Companies | Individuals | Central administration or central banks |
| Banat | 317,974,283 | 463,579 | - |
| Bucharest | 1,828,505,170 | 14,991,468 | - |
| Crisana-Maramures | 200,406,424 | 204,655 | - |
| Dobrogea | 90,998,041 | 3,036,091 | - |
| Moldova | 265,958,706 | 2,194,956 | - |
| Muntenia | 114,372,147 | 721,881 | - |
| Oltenia | 201,383,103 | 928,140 | - |
| Transilvania | 436,818,107 | 1,004,289 | - |
| Total | **3,456,415,980** | **23,545,059** | - |

## Geographical distribution of exposures divided by performance UniCredit Bank – *individual view*

- *RON* -

| Exposure / Geographical Area | 31.12.2016 | | | |
|---|---|---|---|---|
| | On Balance Sheet Exposure | | Off Balance Sheet Exposure | |
| | Impaired loans | Performing loans | Impaired loans | Performing loans |
| | Gross exposure | Gross exposure | Gross exposure | Gross exposure |
| Banat | 83,993,889 | 1,149,426,809 | 32,680,282 | 576,766,353 |
| Bucharest | 1,081,033,403 | 7,529,632,302 | 216,484,458 | 6,795,556,881 |
| Crisana-Maramures | 134,250,808 | 853,102,625 | 20,965,186 | 344,108,784 |
| Dobrogea | 119,041,622 | 853,317,637 | 13,787,799 | 338,104,158 |
| Moldova | 984,023,483 | 2,121,031,570 | 1,837,752 | 1,289,002,655 |
| Muntenia | 106,212,037 | 1,177,193,762 | 28,211,135 | 720,500,811 |
| Oltenia | 116,675,565 | 1,376,376,918 | 10,869,145 | 504,732,783 |
| Transilvania | 149,664,819 | 2,383,246,127 | 13,847,236 | 1,480,896,989 |
| TOTAL | **2,774,895,624** | **17,443,327,751** | **338,682,991** | **12,049,669,413** |

UniCredit Bank

**UniCredit Consumer Financing** – *individual view*

*- RON -*

| Exposure / Geographical Area | 31.12.2016 | | | | | |
|---|---|---|---|---|---|---|
| | On Balance Sheet Exposure | | | Off Balance Sheet Exposure | | |
| | Non-performing Loans | Other Impaired loans | Performing loans | Non-performing Loans | Other Impaired loans | Performing loans |
| | Gross exposure | Gross exposure | Gross exposure | Gross exposure | Gross exposure | Gross Exposure |
| **South** | 505,783 | 6,450,808 | 325,932,508 | - | - | - |
| **Nord** | 618,421 | 5,510,521 | 251,062,413 | - | - | - |
| **East** | 402,053 | 5,799,083 | 426,572,895 | - | - | - |
| **Bucharest** | 1,283,291 | 13,138,225 | 723,400,393 | - | - | - |
| ***TOTAL*** | **2,809,547** | **30,898,637** | **1,726,968,209** | - | - | - |

**Leasing Companies** – *sub-consolidated view*

*- RON -*

| Exposure / Geographical Area | 31.12.2016 | | | |
|---|---|---|---|---|
| | On Balance Sheet Exposure | | Off Balance Sheet Exposure | |
| | Non-performing Loans | Performing loans | Non-performing Loans | Performing loans |
| | Gross exposure | Gross exposure | Gross exposure | Gross exposure |
| Banat | 16,413,661 | 302,024,200 | - | 2,415,691 |
| Bucharest | 426,276,115 | 1,417,220,523 | 347,728 | 268,808,108 |
| Crisana-Maramures | 7,702,457 | 192,908,622 | - | 5,535,553 |
| Dobrogea | 36,132,534 | 57,901,598 | - | 4,386,041 |
| Moldova | 27,049,720 | 241,103,942 | - | 7,279,797 |
| Muntenia | 37,466,392 | 77,627,636 | - | 3,527,800 |
| Oltenia | 16,613,177 | 185,698,066 | - | 2,902,900 |
| Transilvania | 23,431,560 | 414,390,836 | - | 17,299,836 |
| **TOTAL** | **591,085,616** | **2,888,875,424** | **347,728** | **312,155,726** |

UniCredit Bank

## Geographical distribution of past due exposures and of impaired exposures UniCredit Bank – *individual view*

*- RON -*

| Exposure / Geographical Area | 31.12.2016 | | | |
|---|---|---|---|---|
| | Past due exposure* | | Impaired exposure** | |
| | Gross Exposure | Impairment allowance | Gross Exposure | Impairment allowance |
| Banat | 2,528,454 | 113,159 | 116,674,171 | 40,243,924 |
| Bucharest | 9,035,497 | 276,531 | 1,297,517,861 | 719,246,299 |
| Crisana-Maramures | 1,423,248 | 96,035 | 155,215,994 | 88,912,067 |
| Dobrogea | 7,247,994 | 137,811 | 132,829,420 | 74,016,331 |
| Moldova | 4,572,697 | 220,600 | 985,861,235 | 206,622,177 |
| Muntenia | 1,552,825 | 113,635 | 134,423,171 | 68,809,977 |
| Oltenia | 6,485,944 | 416,529 | 127,544,709 | 87,317,717 |
| Transilvania | 7,375,327 | 144,372 | 163,512,055 | 73,404,579 |
| *TOTAL* | **40,221,986** | **1,518,674** | **3,113,578,616** | **1,358,573,071** |

## UniCredit Consumer Financing – *individual view*

*- RON -*

| Exposure / Geographical Area | 31.12.2016 | | | |
|---|---|---|---|---|
| | Past due exposure* | | Impaired exposure** | |
| | Gross Exposure | Impairment allowance | Gross Exposure | Impairment allowance |
| South | - | - | 6,956,591 | 5,586,764 |
| Nord | - | - | 6,128,942 | 4,968,314 |
| East | - | - | 6,201,136 | 4,969,061 |
| Bucharest | - | - | 14,421,516 | 11,644,836 |
| TOTAL | - | - | **33,708,184** | **27,168,975** |

**UniCredit Bank**

**Leasing Companies** – ***sub -consolidated view***

- ***RON -***

| Exposure / Geographical Area | 31.12.2016 | | | |
|---|---|---|---|---|
| | Past due exposure* | | Impaired exposure** | |
| | Gross Exposure | Value adjustments and provisions | Gross Exposure | Value adjustments and provisions |
| Banat | 115,771,239 | 496,206 | 16,413,661 | 12,688,521 |
| Bucharest | 396,688,578 | 3,805,239 | 426,276,115 | 173,551,502 |
| Crisana-Maramures | 66,009,689 | 395,080 | 7,702,457 | 6,116,003 |
| Dobrogea | 18,739,888 | 118,808 | 36,132,534 | 20,650,147 |
| Moldova | 74,207,252 | 446,472 | 27,049,720 | 24,401,588 |
| Muntenia | 12,615,895 | 95,614 | 37,466,392 | 30,058,211 |
| Oltenia | 56,593,041 | 359,012 | 16,613,177 | 14,447,403 |
| Transilvania | 80,390,573 | 640,489 | 23,431,560 | 22,008,895 |
| TOTAL | **821,016,155** | **6,356,920** | **591,085,616** | **303,922,270** |

**) Past due items are those receivables that register overdues (payment delay) and are not impaired*

***) Impaired items - a financial asset or a group of financial assets are impaired and impairment adjustment incur whether objective impairment evidence exist as a result of:*

- *One or many triggers which appeared after initial recognition of the investment (default events);*

*That default event has an impact on estimated future cash flows of the asset which can be reliable measured.*

**UniCredit Bank**

**Distribution of provisions, expenses related to provisions and past due items by business sector**
**UniCredit Bank –** ***individual view***

\- RON -

| Industry | 31.12.2016 | | | | |
|---|---|---|---|---|---|
| | Impairment allowance | Impairment adjustments | Gross credit exposure | Impaired exposure | Past due exposure |
| Private entities (including individuals) | 237,250,514.00 | (23,137,603.00) | 4,899,243,272.00 | 373,691,055.00 | 9,214,172.18 |
| Agriculture, forestry and fishing | 25,153,952.00 | 6,911,228.00 | 1,134,481,565.00 | 28,994,817.00 | 4,556,213.76 |
| Mining and quarrying | 858,424.00 | 275,143.00 | 32,128,648.00 | 982,404.00 | - |
| Manufacturing | 249,432,797.00 | (78,331,969.00) | 4,802,205,150.00 | 357,410,483.00 | 7,010,522.81 |
| Electricity, gas, steam and air conditioning supply | 1,117,848.00 | 620,425.00 | 385,073,174.00 | 17,457.00 | 2,403.48 |
| Water supply | 14,121,764.00 | 8,510,226.00 | 159,201,160.00 | 33,230,577.00 | 103,270.25 |
| Construction | 306,824,423.00 | 88,283,827.00 | 1,002,710,817.00 | 405,244,598.00 | 416,030.42 |
| Wholesale and retail trade | 253,210,772.00 | (23,543,262.00) | 3,430,444,719.00 | 365,600,766.00 | 11,599,864.40 |
| Transport and storage | 20,771,174.00 | 4,546,560.00 | 538,038,677.00 | 27,568,804.00 | 963,731.01 |
| Accommodation and food service activities | 2,128,561.00 | (569,974.00) | 106,143,755.00 | 5,208,063.00 | 1,059,153.84 |
| Information and communication | 21,880,675.00 | 45,054.00 | 640,847,070.00 | 27,677,525.00 | 518,512.23 |
| Financial and Insurance Activities | 925,872.00 | 618,119.00 | 463,152,755.00 | 170,508.00 | 57,584.54 |
| Real estate activities | 138,106,534.00 | (339,273,360.00) | 1,384,840,733.00 | 924,280,974.00 | 47,172.51 |
| Professional, scientific and technical activities | 23,422,942.00 | 14,763,757.00 | 426,297,007.00 | 60,742,621.00 | 195,950.05 |
| Administrative and support service activities | 9,228,490.00 | (4,311,363.00) | 123,777,072.00 | 13,394,388.00 | 30,581.23 |
| Public administration and defence, compulsory social security | 95,684,150.00 | 102,798,022.00 | 598,632,460.00 | 143,226,617.00 | - |
| Education | 2,566,653.00 | 2,387,970.00 | 6,734,364.00 | 3,615,130.00 | - |
| Human health services and social work activities | 706,963.00 | (6,423,978.00) | 36,719,657.00 | 969,831.00 | - |
| Arts, entertainment and recreation | 287,532.00 | (88,926.00) | 10,548,766.00 | 253,779.00 | 60,369.36 |
| Other services | 1,997,862.00 | (72,869,666.00) | 37,002,554.00 | 2,615,227.00 | 113,179.85 |
| *TOTAL* | **1,405,677,902.00** | **(318,789,770.00)** | **20,218,223,375.00** | **2,774,895,624.00** | **35,948,711.92** |

*See more details on Separate Financial Statements for 31.12.2016 - Note 16.*

UniCredit Bank

**UniCredit Consumer Financing – *individual view***

- ***RON -***

| Industry | 31.12.2016 | | | | |
|---|---|---|---|---|---|
| | Impairment allowance | Impairment adjustment | Gross credit exposure | Impaired exposure | Past due exposure |
| Individuals - TOTAL | **66,571,927** | **-** | **1,760,676,394** | **33,708,184** | - |

**Leasing Companies – *sub-consolidated***

- ***RON -***

| Industry | 31.12.2016 | | | | |
|---|---|---|---|---|---|
| | Provisions from credits | Expenses related to provisions | Gross credit exposure | Depreciated exposure | Past due exposure |
| **Agriculture, forestry and fishing** | 24,340,338 | 1,690,287 | 206,247,008 | 38,358,079 | 49,698,181 |
| **Mining and quarrying** | 3,504,661 | 2,440,488 | 27,673,685 | 9,104,328 | 2,685,363 |
| **Manufacturing** | 59,130,783 | 5,121,525 | 511,912,913 | 83,793,717 | 87,301,656 |
| **Energy** | 54,165,361 | 20,086,356 | 212,933,251 | 174,204,108 | 21,402,828 |
| **Water supply** | 3,636,248 | -312,987 | 34,879,842 | 4,904,290 | 4,687,392 |
| **Construction** | 53,271,410 | 734,198 | 285,543,713 | 101,894,890 | 88,927,155 |
| **Wholesale and retail trade** | 52,813,349 | 4,013,755 | 796,869,411 | 65,997,783 | 142,300,712 |
| **Transport and storage** | 34,572,043 | 3,864,339 | 801,319,257 | 47,201,750 | 324,004,866 |
| **Accommodation and food service activities** | 2,432,897 | -561,134 | 50,635,969 | 2,317,797 | 8,201,012 |
| **Information and communication** | 2,765,678 | 701,022 | 33,541,669 | 3,103,493 | 6,259,548 |
| **Financial and insurance activities** | 572,026 | 71,513 | 7,147,706 | 737,817 | 1,600,858 |
| **Real estate activities** | 3,538,882 | 1,026,023 | 142,945,589 | 4,075,491 | 21,373,088 |
| **Professional, scientific and technical activities** | 15,328,692 | 1,027,566 | 145,015,714 | 42,636,775 | 22,813,622 |
| **Administrative and support service activities** | 7,111,790 | 26,809 | 105,161,805 | 8,286,102 | 19,664,491 |
| **Public administration and defence, compulsory social security** | 10,908 | 60 | 3,265,354 | 0 | 602,449 |
| **Education** | 136,186 | 45,955 | 3,924,449 | 98,559 | 1,251,564 |
| **Human health services and social work activities** | 1,103,763 | 258,757 | 67,774,359 | 557,774 | 9,923,839 |
| **Arts, entertainment and recreation** | 948,493 | 37,827 | 8,017,769 | 1,144,219 | 1,213,565 |
| **Other (including Individuals)** | 2,892,980 | 769,833 | 35,151,576 | 2,668,646 | 7,103,965 |
| **TOTAL** | **322,276,485** | **41,042,191** | **3,479,961,040** | **591,085,616** | **821,016,155** |

**Total exposures after accounting offsets and without taking into account the effects of credit risk mitigation, broken down by different types of exposure classes, impairment allowance,net exposure of impairment allowance, risk weighted assets, at consolidated level.**

*- RON –*

| CREDIT AND COUNTERPARTY RISK | 31.12.2016 | | | |
|---|---|---|---|---|
| | Gross Exposure | Impairment allowance | Net exposure | Risk weighted exposure |
| *STANDARDISED APPROACH* | **28,676,290,345** | **1,437,629,045** | **27,238,661,300** | **10,167,891,375** |
| 1.Central administration or central banks | 10,071,754,499 | 14,747 | 10,071,739,752 | 97,172,254 |
| 2.Regional administration or local authorities | 566,688,782 | 268,883 | 566,419,899 | 204,371,509 |
| 3.Institutions | 792,027 | 9,021 | 783,006 | 110,136,265 |
| 4.Corporates | 4,153,087,538 | 17,157,012 | 4,135,930,526 | 2,912,043,608 |
| 5.Retail | 5,767,004,878 | 76,266,608 | 5,690,738,270 | 3,212,941,618 |
| 6.Exposures secured by mortgages on immovable property | 3,751,162,600 | 11,984,753 | 3,739,177,847 | 1,456,331,270 |
| 7.Exposures in default | 2,587,627,831 | 1,013,052,939 | 1,574,574,892 | 1,578,959,855 |
| 8.Exposures associated with particularly high risk | 135,277,383 | 97,724,731 | 37,552,652 | 56,328,978 |
| 9.Equity exposures | 6,147,236 | 1,117,979 | 5,029,257 | 5,029,257 |
| 10.Exposures to institutions and corporate with short term credit assessments | 45,466,757 | - | 45,466,757 | 9,093,352 |
| 11.Assets, other than those that represent credit exposures | 1,591,280,814 | 220,032,372 | 1,371,248,442 | 525,483,409 |
| *INTERNAL RATING BASED APPROACH* | **23,356,562,805** | **742,679,558** | **22,613,883,247** | **12,591,613,147** |
| 1.Central administration or central banks | 986,806,840 | 122,206,205 | 864,600,635 | 432,691,777 |
| 2.Institutions | 2,540,057,247 | 439,186 | 2,539,618,061 | 829,597,665 |
| 3.Corporates | 19,829,698,718 | 620,034,167 | 19,209,664,551 | 11,329,323,705 |
| *EQUITY EXPOSURES ACCORDING TO INTERNAL RATING BASED APPROACH* | **15,251,263** | - | **15,251,263** | **56,429,672** |
| *TOTAL* | **52,048,104,413** | **2,180,308,603** | **49,867,795,810** | **22,815,934,194** |

*Note: The classification is realised based on exposure classes defined by Regulation no. 575/2013 of European Parliament and Council regarding prudential requirements for credit institutions and investment companies and amending Regulation (UE) no.648 / 2012.*

### *5.4. Credit risk impaired/NLPs policies*

A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future CF of the financial asset or group of financial assets that can be reliably estimated. It may not be possible to identify a single, discrete event that caused the impairment. Rather the combined effect of several events may have caused the impairment.

At the end of each reporting period the Bank evaluates whether there is any objective evidence that a financial asset or group of financial assets is impaired.

### 5.5. *Stress testing disclosure*

Stress testing program is an integral part of the Bank's risk management framework, being supported by an effective infrastructure to perform stress tests depending on the nature, scale and complexity of the activities, and also depending on the risk profile.

The management body has the final responsibility for the credit institution's overall stress testing program.

The Bank uses stress testing as a diagnostic tool to understand their risk profile and as a forward-looking tool within the internal capital adequacy assessment process - for example, to assess how the profits are affected by crisis situations, for internal assessment of capital adequacy, or for risk assessment in an anticipatory measure.

In general a capital stress test assumes possible but uncertain scenarios, based on assumptions of the development of the capital market. This leads to different effects and impact on the Capital components. It shows whether the bank is able to stay over the regulatory minimum of Capital requirement under adverse conditions.

Bank running periodically stress tests based on the different stressed scenarios, with different level of severity, defined by Holding Company.

### 5.6. *Credit risk impaired/NLPs opening vs closing balances*

**Credit Risk Adjustments – Approaches and Methods**

**Approaches and methods applied for the calculation of prudential adjustments of value - for the credit portfolio under the Standardised Approach.**

In order to cover potential credit and investment losses, the Bank calculates prudential adjustments of value according to the National Bank of Romania regulations in force.

Consequently, for the determination of the level for prudential adjustments of value, the credit exposures are classified based on the following elements:

- Obligor financial performance category;
- Delinquency (number of overdue days);
- Initiation of judicial procedures.

The obligor financial performance category, used for establishing the risk class in accordance with National Bank of Romania regulations for determining credit risk adjustments, is determined based on internal assessment systems / methodologies considering qualitative and quantitative factors.

The specific value adjustments are determined by applying the coefficients of each risk category to the exposure adjusted with the available eligible collaterals. The eligibility of the collaterals is considered in alignment with the provisions of the National Bank of Romania norms regarding the calculation of the specific risk value adjustments.

**Approaches and methods applied for the calculation of value adjustments**

Provisions represent the loss amount estimated by the Bank based on impairment models. The Bank uses two approaches for this estimation:

- Individual assessment
- Collective assessment

In collective assessment, the provisions are calculated at portfolio level by dividing it into buckets with similar credit risk characteristics. The performing portfolio is entirely subject to collective assessment, irrespective if the exposures are considered significant or not. The non-performing portfolio is subject to collective assessment only in the in case the exposures are not considered significant.

In individual assessment, the provisions are individually calculated for each individually significant exposure. Individual assessment is a process of measurement of impaired exposure for an individual client. According to IAS39, individual assessment is required for individually significant exposures and may also be used to assess exposures not considered significant.

The individual assessment process is divided into two steps:

- Identification of individually significant exposures and/or exposures of clients which may be individually assessed
- Individual loss estimation for provisioning purpose for the respective exposures.

**Individually significant impaired loans**

Individually significant impaired loans comprises significant private individuals (more than EUR 250,000) which have at least one default event, as defined in the Bank's internal procedures, and significant corporate clients (more than EUR 1 million) with grade 8-, 9 or 10, as defined in the internal rating of the Bank; these two categories are individually assessed by the Bank.

For all of them, the collaterals are divided between property, goods, assignment of receivables and other. Other collateral includes pledge on stocks, machinery, cash and financial risk insurance.

**Other impaired loans**

Other impaired loans include all loans to individuals with more than 90 days late and credits to businesses with grades 8, 9 and 10 that are not individually significant.

### Past due but not impaired loans

Loans with overdue contractual interest or principal cash flows which are not considered impaired due to the level of guarantees available or/and the stage of the collection of the amounts by the Bank.

### Neither past due nor individually impaired

It includes all exposures not classified in the above categories and considered to be all performing.

### Allowances for impairment

Set out below is an analysis of the gross and net (of allowances for impairment) amounts of individually impaired assets by risk grade:

| 31 December 2016 | Gross amounts | Net amounts |
|---|---|---|
| *In RON* | | |
| Grade 8-: Impaired | 2,119,936,380.44 | 1,301,555,800.81 |
| Grade 9: Impaired | 173,556,213.10 | 32,606,631.39 |
| Grade 10: Impaired | 481,403,030.77 | 124,075,072.81 |
| **Total** | **2,774,895,624.31** | **1,458,237,505.01** |

| 31 December 2015 | Gross amounts | Net amounts |
|---|---|---|
| *In RON* | | |
| Grade 8-: Impaired | 2,635,109,111 | 1,645,504,476 |
| Grade 9: Impaired | 220,213,215 | 68,252,362 |
| Grade 10: Impaired | 694,821,237 | 182,341,659 |
| **Total** | **3,550,143,599** | **1,896,098,497** |

### *5.7. RWA calculation method and models*

For calculating the RWA for credit risk, the Bank applies the Foundation Internal Rating Based Approach, according to Regulation no. 575/ 2013 of European Parliament and Council dated 26.06.2013 regarding prudential requirements for credit institutions and investment companies and amending Regulation (UE) no.648/ 2012 of the Comission for establishing technical standards for reporting for supervisory purposes and by Regulation no. 5/ 2013 regarding prudential requirements for credit institutions issued by National Bank of Romania (due to the joint approval received from Bank of Italy, FMA and National Bank of Romania) for the following segments of clients: corporate (except for real estate clients and specialized financing), multinational companies, banks and securities industries. For the rest of the portfolio, the Bank continued to use the standardized approach.

### 5.8. RWA - IRB by internal rating grade

In July 2012, National Bank of Romania authorized the Bank to calculate the credit risk capital requirement under Foundation IRB Approach for the following categories of clients: corporate (except for real estate clients), multinationals, banks and securities industries. For the rest of the portfolios, the Bank is still applying the Standardized Approach.

The Bank uses internal rating models for estimation of probability of default.

Structure of internal ratings:

| Exposure Class | Rating System | Type |
|---|---|---|
| Central governments and central banks | Sovereign (PD) | Group Model |
| Institutions | Banks (PD) | Group Model |
| Corporate - Multinationals | Multinational (PD) | Group Model |
| Corporate (excluding Real Estate) | Mid Corporate (PD) | Local Model |

Rating Scale – relationship between internal and external ratings

| Rating Class | Rating Notch | S&P | Moody's | Fitch |
|---|---|---|---|---|
| 1 | | AAA/AA+...AA | Aaa/Aa1...Aa3 | AAA / AA+ |
| 2 | | A+ ... A- | A1 ... A3 | A+ ...A- |
| 3 | | BBB+/BBB | Baa1/Baa2 | BBB+/BBB |
| 4 | | BBB-/ BB+ | Baa3... Ba1 | BBB-/BB+ |
| 5 | | BB | Ba2 | BB |
| 6 | | BB/B+ | Ba3/B1 | BB/B+ |
| 7 | | B | B2 | B |
| 8 | 8+ | B- | B3 | B- |
| | 8 | CCC/CC | Caa/Ca | CCC/CC |
| | 8- | | | |
| 9 | 9 | | | |
| 10 | 10 | | | |

Internal rating models and risk estimates are used for calculating risk-weighted exposure and also for other purposes related to credit risk management: strategies definition, budgeting process, assessment proces, decision process, pricing, monitoring, reporting and portfolio management, stress testing and process for identification of problem assets.

The inputs for risk parameters estimates should be essentially the same both, for credit management purposes and for regulatory capital requirement calculation purposes. Any differences between the ratings and risk parameter estimates used in calculating capital requirements and the final parameters used internally shall rely on a well documented rationale.

In accordance with internal regulation and taking into account Group guidelines, the Bank implemented processes for the development of internal rating models, and also processes that ensure a periodical cycle for internal model validation, that include monitoring of model performance and stability, review of model specification, and testing of model outputs against outcomes.

Any rating model supposes the following stages:

- rating model development
- initial validation
- monitoring of the rating model
- rating model refinement
- on-going validation

### *5.9. RWA – Backtesting*

RWA backtesting is covered by validation activities with regard to internal Rating systems.

### *5.10. Credit risk mitigation*

**Qualitative Information**

The goal of providing collateral is to minimize the loss given default (credit risk) by diminishing the loss or risk transfer, as follows:

- For real collateral, financial or physical, the risk exposure is reduced by the expected revenue to be realised from collateral valorification and, thus, losses can be reduced;
- For collateral provided by means of letters of guarantee or other personal guarantees, the risk is transferred to the protection provider.

The Bank established the accepted collateral types and also the conditions for the collateral acceptance.

For a better administration of all collateral instruments accepted in the credit process and for a better mitigation of associated risks, the Bank has implemented within internal credit management system, a specific collateral module where all accepted collateral instruments are adequately, uniformly recorded and managed in a structured manner. Adequate data quality is ensured by processes and controls supported by the system.

Collateral management system ensures:

- Monitoring and controlling of collaterals;
- Estimation of loss given default;
- Calculation of collateral recovery rates;
- Production of various portfolio analyses.

Considering the mitigation of risk exposure for determining the minimum capital requirements, the Bank is using eligible collaterals according to National Bank of Romania Regulation no. 5/20.12.2013 regarding prudential requirements for credit institutions and Regulation no. 575/2013 of European Parliament and Council regarding prudential requirements for credit institutions and investment companies and amending Regulation (UE) no.648 / 2012.

Collateral types accepted by the Bank as credit risk mitigation techniques for calculating the minimum capital requirements according to the standardized approach Basel III, are presented below:

| Collateral Category | | Type of collateral |
|---|---|---|
| **Direct Personal Guarantees** | | Guarantee / Surety |
| | | Bill of exchange from third party |
| | | Letter of comfort |
| | | Risk sharing |
| **Credit Derivatives** | | Credit Derivatives Instruments |
| **Life Insurance** | | Pledge on life inssurance with non reducible surrender value |
| **Financial collateral** | Own | Pledge on securities deposits |
| | | Pledge on cash collateral |
| | | Pledge on gold |
| | Third Party | Pledge on third party cash collateral |
| **Residential Real Estate** | | First Rank Mortgage on RRE occupied or rented by owner |
| **On Balance Sheet Netting** | | Not used in the Bank as credit risk mitigation technique |

Collateral types accepted by the Bank as credit risk mitigation techniques for computing the minimum capital requirements according to the internal rating based approach Basel III, are those considered under standardized approach and the ones that are presented below:

| Collateral Category | Type of collateral |
|---|---|
| **Commercial Real Estate** | First rank mortgage on commercial real estate – offices and other commercial spaces |
| **Moveable collateral** | Receivables on commercial transactions or transactions with initial maturity less or equal to one year |
| **Other categories of tangible goods** | Not used in the Bank as credit risk mitigation techniques |

**Policies and processes applied for evaluating and administrating real collaterals**

The internal Bank value calculation is carried out by experts, who have the required qualifications, ability, experience and competence to perform such a valuation and who are independent of the credit decision.

The valuation of the goods proposed as collateral shall be made by independent valuators approved by UniCredit Bank or by the Bank's internal valuators.

The internal and independent valuators must be certified by A.N.E.V.A.R. and the valuation reports need to comply with relevant Valuation Standards in force.

The valuation report is the document that attests the valuation result, namely the material value of the collateral depending on which the collateral coverage corresponding to a lending operation is calculated.

If collateral is accepted in a currency that differs from that of the credit and/or if the collateral is not available for the entire credit maturity, under certain conditions, for minimum capital requirements calculation purpose, the collateral values are to be reduced accordingly as per Basel III legal requirements.

**Quantitative Information**

| Risk Classes | 31.12.2016 | | | |
|---|---|---|---|---|
| | Financial collaterals | Personal collaterals | Receivables | Commercial real estate |
| *STANDARDIZED APPROACH* | | | | |
| 1.Central administration or central banks | - | - | - | - |
| 2.Regional administration or local authorities | - | - | - | - |
| 3.Institutions | 3,863 | - | - | - |
| 4.Corporates | 279,293,825 | 38,867,606 | - | - |
| 5.Retail | 56,516,290 | 157,886,076 | - | - |
| 6.Exposures secured by mortgages on immovable property | - | - | - | - |
| 7.Exposures in default | 279,078,416 | 7,403,918 | - | - |
| 8.Exposures associated with particularly high risk | - | - | - | - |
| 9.Equity exposures | - | - | - | - |
| 10.Exposures to institutions and corporate with short term credit assessments | - | - | - | - |
| 11.Assets, other than those that represent credit exposures | - | - | - | - |
| *INTERNAL RATING BASED APPROACH* | | | | |
| 1.Central administration or central banks | - | - | - | - |
| 2.Institutions | 874,470,385 | 22,143,803 | 345,477,736 | 1,250,308 |
| 3.Corporates | 223,748,838 | 480,825,104 | 2,111,003,553 | 1,123,843,933 |
| *TOTAL* | **1,713,111,617** | **707,126,505** | **2,456,481,289** | **1,125,094,241** |

*Notes:*

1. *The classification is realised based on exposure classes defined by Regulation no. 575/2013 of European Parliament and Council regarding prudential requirements for credit institutions and investment companies and amending Regulation (UE) no.648 / 2012;*
2. *Includes besides credit risk adjustments also the value adjustments / provisions reported to National Bank of Romania in COREP.*

# 6. Exposure to counterparty risk

## *6.1. Limits on exposures, policies for assessing counterparty credit risk and guarantee risk, management of wrong - way risk etc.*

Counterparty credit risk is measured and monitored by an independent risk management unit using an internal model based on historical simulation.

Counterparty credit risk is classified into two categories:

- Pre-settlement risk (risk that a counterparty defaults prior to termination of the deal);

- Settlement risk (risk that a counterparty defaults in the time when contractual payments are due whereby payments/deliveries to the counterparty already took place before counter value has been received.

Counterparty risk monitoring is based on a system of limits for individual counterparties and product groups (spot, derivatives, money market, securities and repo).

The Bank does not hold credit derivatives hedges.

## *6.2. Positive fair value of financial and credit derivatives, collateral held, value of CCF etc.*

Details regarding the fair value of derivatives, notional value of trading contracts and notional value of hedging contracts that are taken into account in own funds calculation at consolidated level, are presented below:

| Derivate Instruments | STANDARDIZED APPROACH | | INTERNAL RATING BASED APPROACH | | Total |
|---|---|---|---|---|---|
| | Corporate | Retail | Corpoarte | Retail | |
| Positive Fair Value | 50,072,976 | 47,886 | 73,125,338 | - | **123,246,200** |
| Notional Trading Derivatives Instruments | 731,861,972 | 4,362,423 | 6,738,104,337 | - | **7,474,328,733** |
| Notional Hedging Derivatives Instruments | - | - | 1,657,084,940 | - | **1,657,084,940** |

# 7. Market risks

## *7.1. Price risk, Interest rate risk, exchange rate risk and credit spread - Trading book*

Trading Book includes all positions in financial instruments owned by UniCredit Bank for trading or hedging the other elements of the trading book that are free from other restrictive clauses on trading opportunities that can be immunized.

Positions held for trading are those held for sale in the short term with the intent to benefit from the difference between purchase price and the sale or short-term fluctuations in interest rates or prices. The term "position" includes both its own positions and those of its clients, and positions resulted from the market maker.

Trading Book of UniCredit Bank contains all products traded as they were approved by the Group:

1. Derivatives exchange rate:
   a) Outright Forwards and FX Swaps;
   b) Plain Vanilla Options;
   c) Exotic FX Options (Digitals and Barriers).
2. Interest rate derivatives:
   a) Interest Rate Swaps (IRS), Cross Currency Swaps (CCS);
   b) Interest Rate Options (Caps, Floors, collars).
3. Commodities derivatives
   a) Swaps
   b) Options
4. Fixed income financial instruments

All other products are part of the Banking Book.

Derivatives are recorded at market value through the daily mark-to-market revaluation.

From the perspective of market risk, all derivatives transactions (except outright forwards and interest rate swaps) are closed back-to-back with another entity within the Group, in most cases, so not having open positions for UniCredit Bank trading activity.

Capital requirements for market risk is calculated using the standardardized method.

**A. Interest Rate Risk**

Interest rate risk arising from Trading Book results from positions in derivative products or fixed income financial instruments of UniCredit Bank. All derivative client transactions (except FX Swaps and FX FWD Outright) are closed back-to-back with another entity owned by UniCredit Group.

Interest rate risk in Banking book is separately measured and monitored by VaR and BPV indicators.

**B. Price Risk**

Price risk results from the activity of capital markets, commodities and associated derivative is zero because UniCredit Bank has no position on these markets / instruments.

**C. Exchange Rate Risk**

Foreign exchange risk arising from positions taken by departments / traders specializing owning specific limits for market risk. This risk arising from trading activities conducted through negotiation on various market instruments and is constantly monitored and measured.

Given the structure of the Banking Book and Trading Book, in the standard method to calculate the capital requirement for position risk (MKR SA TDI form) and for foreign exchange (MKR SA FX form) based on open currency positions at the end of each month, and reported by the National Bank of Romania.

The amount of capital requirement is determined based on regulations in force.

The following risk limits are also monitored:

- FX net open position limits;
- BPV limits (Basis Point Value);
- CPV limits (Credit Point Value);
- VaR limits (Value at Risk);
- LWL limits (Loss Warning Level);
- Liquidity limits (Trigger points / Ratios);
- Limits for investments in government securities.

**Stress Tesing**

The market risk profile, is monitored for the following crisis scenarios:

- Currency risk - run locally and within market risk management system;
- Interest rate risk - run locally and within market risk management system;
- Credit spread risk – run within market risk management system;
- Short term liquidity – run locally and within the liquidity system;
- Economic capital – run quarterly at local level and in the market risk system.

### *7.2. Price risk, interest rate risk, exchange rate risk - Banking book*

Interest rate risk consists of changes in interest rates that are reflected in:

- Interest income sources, and thus, the Bank's earnings (cash flow risk);
- The net present value of assets and liabilities, due to their impact on the present value of future cash flows (fair value risk).

The Bank measures and monitors interest rate risk on a daily basis within the framework of its Banking Book interest rate risk policy which defines methods and corresponding limits or thresholds of interest margin sensitivity and economic value.

Interest rate risk affects all proprietary positions arising out of business operations and strategic investment decisions (Banking Book).

The main sources of interest rate risk can be classified as follows:

- Re-pricing risk: the risk resulting from maturity and re-pricing mismatches of the Bank's assets and liabilities. The main components of this risk are:
  - Yield curve risk: risk resulting from exposure of the Bank's positions to changes in the slope and shape of the yield curve;
  - Basis risk: risk resulting from the imperfect correlation in lending and borrowing interest rate changes for different instruments that show similar re-pricing characteristics;
- Optionality risk: risk resulting from implicit or explicit options in the institution's banking book positions.

The Bank set limits to reflect the risk appetite consistent with the strategic guidelines issued by the Group and the Management Board. These limits are defined in terms of VaR, sensitivity or re-pricing gap.

The risk management for interest rate risk on positions in Banking Book management of is realised by the sterilization of Bank's balance sheet risk in terms of notional interest by meeting the limits set.

The independent risk unit establishes risk limits and verifies the utilisation on a daily basis.

### *7.3. Stress testing disclosures*

Market Risk performs the following stress tests, which are presented in the Risk Management Operative Committee, Assets & Liabilities Committe and Supervisory Board:

<u>**Currency Risk**:</u>

a) Daily calculation of the impact of +/- 10% change of the fx rate
b) Monthly calculation of the impact of the following scenarios:
   - depreciation EUR vs all other currencies with -15%
   - appreciation EUR vs all other currencies with +15%
   - depreciation EUR vs all other currencies with -10%
   - appreciation EUR vs all other currencies with +10%

   - depreciation RON vs EUR with -15%
   - appreciation RON vs EUR with +15%
   - depreciation RON vs EUR with -10%
   - appreciation RON vs EUR with +10%

   - depreciation USD vs EUR with -15%
   - appreciation USD vs EUR with +15%
   - depreciation USD vs EUR with -10%

- appreciation USD vs EUR with +10%

**Interest rate risk**

In order to quantify the potential modification of economic value as a result of shifts in interest rate curves, the following aspects are taken into account:

a) daily calculation by Market Risk department of the sensitivity of 1 bp on FX Forward *(DV01)
b) daily analysis of the impact of 1 bp shift for bonds portfolio
c) using the following scenarios for quantifying the modification of economic value in extreme conditions (stress tests) –calculation in the market risk system of the impact of the following scenarios:
    - scenario 1: parallel shift +100bps, all currencies
    - scenario 2: parallel shift -100bps, all currencies
    - scenario 3: parallel shift +200bps, all currencies
    - scenario 4: parallel shift -200bps, all currencies
    - scenario 5: RON O/N to 1Week: -500bps<br>RON 1Week and above: +50bps<br>all other currencies: unchanged
    - scenario 6: RON O/N to 1Week: +500bps<br>RON 1Week and above: +50bps<br>all other currencies: unchanged
    - other stress scenarios

**Credit spread risk**

- scenario 1: parallel shift +50bps for the bonds portfolio;
- scenario 2: parallel shift +100bps for the bonds portfolio;
- scenario 3: parallel shift +200bps for tghe bonds portfolio

**Economic capital**

Scenarios with different probabilities and severities as fromalized in internal procedures.

The economic capital for Market Risk is computed based on the Group developed IMOD Model, which is based on the Value at Risk (VaR) methodology.

**Liquidity Risk**

Scenarios developed by the Group as well as internal developed scenarios which consider several degrees of liquidity crisis, as formalized in internal procedures.

### 7.4. RWA calculation method and models

For calculating the RWA for market risk, the Bank applies the Standardized Approach, according to Regulation no. 575/ 2013 of European Parliament and Council dated 26.06.2013 regarding prudential requirements for credit institutions and investment companies.

### 7.5. Risk Management organization

Generally, a banks' market risks are due to price fluctuations or other market risk factors affecting the value of positions on its own books, both trading book and banking book, i.e. those arising from transactions and strategic investment decisions.

UniCredit Bank produces detailed reports on business trends and related risks on a daily basis, forwarding market risk documentation to local management, local authorities and relevant structures in the Group.

The relevant structures at Group level lay down strategic guidelines for taking on market risks by calculating, depending on risk appetite and objectives of value creation in proportion to risks assumed, capital allocation for the Parent company and its subsidiaries.

The relevant structures at Group level propose limits and investment policies for the Group and its entities in harmony with the capital allocation process when the annual budget is drawn up. Group Asset and Liability Management unit, in coordination with other regional liquidity centers, manages strategic and operational activities, with the objective of ensuring a balanced asset position and the operating and financial sustainability of the Group's growth policies on the loans market, optimizing the exchange rate risk, interest rate risk and liquidity risk.

Market Risk Management activity is performed according to legal regulations in force in Romania, norms and regulations issued by the National Bank of Romania (NBR) and internal regulations of UniCredit Bank, while the application of these regulations is harmonized with the Group Rules of UniCredit.

In UniCredit Bank, **Market Risk management function** is organized at centralized level in the Risk Division – Market Risk department.
According to Regulation no 5/2013 on prudential requirements for credit institutions, the following definitions are presented:

- **Market risk** is the risk of incurring on-balance and off-balance sheet losses due to adverse market movements in prices (such as, for example, the share prices, the interest rates, the foreign-exchange rates)
- **Interest rate risk** is the current or future risk of negative impact on profits and capital as a consequence of certain adverse changes of the interest rates
- **Liquidity risk** is the current or future risk of negative impact on profits and capital, determined by the credit institution's inability to meet its liabilities when they become due

The market risk mangement activity is regulated by a specific set of policies and procedures for the purpose of:

- Identifying, monitoring, analysis and controling market risks: currency risk, interest rate and liquidity, according to Group standards and requirements of the National Bank of Romania through a system of limits for both the trading portfolio (trading book) and for positions outside the trading portfolio (banking book);
- Implementing the strategy of market risk management through appropriate policies and processes;
- Reporting of market risk issues to Bank's management.

Market risk management strategy is accomplished by applying the following principles:

- Market risk management will be achieved through specific risk indicators and models such as VaR limits, limits BPV, Loss Warning Level limits, foreign exchange position limits (the limits that define the Bank's risk profile );
- Trading positions will be held at current market value (mark-to-market). If specific revaluation models are used, they will be validated independently;
- All relevant risk factors will be identified and considered during the process of limits setting.
- Specific events will be considered in the stress scenarios, not as manual adjustment of volatility or correlations amoung risk factors;
- VAR calculation includes all Bank activity, not only specific positions in the trading book; also, VaR Banking Book and VaR Trading Book is calculated and monitored separately, inclusive per risk factors;
- Exposure to market risk (usage of limits, excesses) will be reported in time and regularly to the respective lines of business, the management and the Group. Risk reports will be generated separately for each risk generating unit.

## 8. Operational risk

### *8.1. Risk Management organization*

The management of operational risk within UniCredit Bank is conducted in line with the internal framework and in compliance with legal and Group regulations in force.

Operational Risk is considered a significant risk and it is integrated into the Bank's policy and strategy regarding significant risks.

**Operational risk** means the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk includes legal risk, but excludes strategic and reputational risk. Legal risk includes, but is not limited to, exposure to fines, penalties or punitive damages resulting from supervisory actions, as well as private settlements.

The main roles and responsibilities in managing and controlling operational risk are attributed to the Supervisory Board, the Management Board, the Superior Management (Directors and Heads of Departments), Bank's committees with responsibilities regarding operational risk, Operational and Reputational Risk function.

Operational and Reputational Risk function is an independent structure in charge with operational risk control, within the Risk Division and reporting directly to the Market and Operational & Reputational Risk Director, who is subordinated to the Chief Risk Officer.

The Management Board and the Supervisory Board of UniCredit Bank have approved the Group Operational Risk Framework.

The framework for operational risk management in UniCredit Bank is well structured and involves relevant factors in promoting a culture favourable to the communication and control of operational risk. The framework is sustained by the existence of a dedicated idependent function for the control of operational risk, by the structure of the relevant committees and by the system of reporting operational risk to the Management of the Bank.

The Bank has a well formalized system of evaluation and management of operational risk, with clear and well defined responsibilities.

The system of operational risk management is integrated into the internal processes for management of significant risks, according to the internal procedures and regulations regarding the management of significant risks.

The main tools employed for the management and control of operational risk in UniCredit Bank are internal operational risk events collection, scenario analysis, operational risk indicators, mitigation actions and operational risk reporting.

**Collection of operational risk internal events** is a main source for the identification and quantification of operational risks. The process of collecting loss events is established through well defined rules for collection, validation and reconciliation of the loss data against accounting bookings, in order to ensure completeness, accuracy and timeliness of reported data. The responsibilities regarding operational risk reporting across the bank are included in the operational risk framework and as well in the procedures specific to each area of activity.

The completeness and accuracy of the operational risk database is ensured through the analysis and reconciliation of internal accounts, according to the process described in the Rules regarding operational risk loss data, collection and control.

**Scenario analysis** is a core element of the Group operational risk control methodology since scenarios aim at providing a forward looking evaluation of Bank's risk profile and improving the understanding for the management of its risk profile by: assessing the impact on the business of hypothetical, yet foreseeable, extreme operational loss events; assessing how bad things could get across a range of stressed conditions;

identifying the best responses to serious threats; identifying areas where controls are missing or could be enhanced.

Scenarios are also used as one of the primary inputs to estimate the Bank's overall risk profile and, whether it has adequate amounts of capital to cushion, the impact of unexpected operational loss events. The metrics derived from the scenarios are used as input into the model, which supports the definition of the Group risk profile on an aggregate basis.

In 2016, scenario analysis was performed according to Group instructions and legal regulations in force.

**Operational risk indicators** reflect the operational risk profile and are correlated to changes in the risk environment. The monitoring of the operational risk indicators plays the role of an early warning system for changes in the operational risk exposure.

During 2016 the operational risk indicators system and the critical monitoring thresholds were revised in order to: identify and set up new indicators relevant for operational risk reporting, align existing thresholds with various risk levels across the Bank and remove the indicators which are no longer relevant in terms of operational risk. To increase efficiency of the risk monitoring, there were defined fixed thresholds for all the indicators considered for capital calculation (Key Risk Indicators).

At the Bank's level there are **periodical reports** regarding the exposure to operational risk, with a focus on: financial losses (including provisions) detailed on event types/model risk categories and business lines, operational risk losses limit usage, capital requirement for operational risk, cross credit events, mitigation actions regarding operational risk discussed in the Permanent Work Group Committees, Key Risk Indicators, thresholds breaches and actions taken, scenarios performed.

The reporting system ensures, at least quarterly, that reports regarding operational risk are communicated to the relevant structures and persons.

The reporting system includes quarterly reports to the Risk Management Operative Committee, at least bi-annually reports to the Supervisory Board and reports to the Operational Risk Committee of Bank Austria. The operational risk reports have a consistent structure and present an overall picture of the exposure to operational risk.

The **capital requirement for operational risk** for UniCredit Bank is determined using the new Advance Measurement Approach (AMA) model adopted in 2014. New AMA model has higher model granularity & risk sensitivity, increased underlying data and stronger focus on forward-looking risk analyses.

The calculation model was applied to the perimeter composed by the Legal Entities authorized to adopt the Advanced Measurement Approach, including UniCredit Bank.

As risk transfer mechanisms, UniCredit Bank uses a Banker's Blanket Bond policy (part of UniCredit Group BBB Policy) that coveres, according with terms and conditions specified in the policy, Financial Organisation Crime, Electronic and Computer Crime, Professional Indemnity. The BBB Policy is complying with the international requirements regarding the use of policies as risk transfer mechanism in order to reduce the capital requirement for operational risk calculated according with AMA.

The calculation of economic capital for operational risk is also based on the AMA model.

### *8.2. Stress testing disclosures*

The stress testing exercise in UniCredit Bank Romania consist of:

**1. Stressed Economic Capital for Operational risk:** calculated by applying a 15% add-on to the baseline Value-at-Risk at the applicable confidence level according to the method suggested for the EBA stress testing 2011.

Since there is still a lack of profound empirical evidence, proofing a correlation between macro-economic parameters and operational risk loss occurrence, the effect of changes in macroeconomic parameters and their influence on operational risk loss frequency and severity currently remains in the unkonwn. Thus, the calculation of stress scenario loss contribution of operational risk to the Pillar 2 Overall Stress Testing process is conducted annually, irrespective of changes of the underlying macro-economic stress scenario.

**2. Stressed loss/ Conditional Loss:** Operational & Reputational Risk Function is in charge of evaluating and reviewing the operational risk stress testing methodology and approach. An annual calculation based on a quantitative as well as a qualitative component is conducted:

- Quantitative loss component: which takes into account the historical operational risk lossess for 10 years time frame.
- Qualitative loss component: which is based on scenario analysis process, taking into account different scenarios for each operational risk event type and losses are valuated for different probabilities of occurrence.

### *8.3. RWA calculation method and models*

The capital calculation within UniCredit Bank Romania is performed according to the AMA model and the figures are as follows:

| Operational Risk RWA 2016 (EUR) | Capital Requirement for Operational Risk (EUR) | |
|---|---|---|
| | 2016 | 2015 |
| 343,643,351 | 27,491,468 | 30,068,051 |

### *8.4. Other risks - Risk types and risk management*

**Fraud risk management** is a prime responsibility for all employees steming from the necessity of protecting UniCredit Bank and its assets / activities from being target to fraudulent activities. The internal framework is aimed at creating an appropriate level of awareness to all employees and partners and to ensure an efficient system of controls to prevent this risk in all aspects included in the circuit of fraud: prevention, detection, investigation and settlement of high risk events, recovery of fraud related losses and the implementation of the necessary corrections.

The fraud risk management was set as a top priority for UniCredit Bank and its coordination is ensured by the Fraud Prevention, Antifraud Departments and Fraud Committee. An ongoing four steps program covering methodology, training, activities' review from a fraud risk perspective and monitoring was implemented to mitigate the likelihood and impact of this risk.

One of the main topics for the Operational Risk strategy is **cybercrime risk** with an enhanced focus on the area of online banking fraud with the related topics phishing/hacking/malware etc. and how the bank can decrease risks in current and upcoming online banking processes.

The **legal risk management** within UniCredit Bank Romania is ensured by all employees with the appropriate assistance and support of the Legal function. The aim of the legal framework is to ensure the adequacy of legal and corporate fulfilments, the examination of the evolution of laws and their consistent interpretation, as well as the identification, assessment and monitoring of the overall legal risks.

**Outsourcing risk** is managed by the competent / involved structures with the appropriate support and oversight of the Risk Management function and dedicated Risk Management Committee. The management of the risks associated with the outsourced activities covers all the outsourcing stages (new initiatives and modifications of existing ones, supplier selection, contract terms and conditions, monitoring of existing outsourced activities, unexpected situations and continuity plans, relation with authorities).

**Business continuity management** represents a critical success factor for UniCredit Bank and it takes a central role in the overall company strategy/goals. The constantly changing threat potential demands a systematic, flexible, integrated and business oriented treatment of business continuity management in UniCredit Bank

The management of the business continuity risk is an ongoing process being the responsibility of management at all levels and of each employee. It is carried out in line with the local UniCredit Bank policies and procedures compliant with Group policies, local legal framework and internationally accepted best practices and standards (ISO 22301).

### *8.5. Other risks - Publicly known risk events*

During 2016 there were no publicly known events which to adversely impact the activity or the reputation of the UniCredit Bank Romania.

# 9. Equity exposures

## *9.1. Description of the bank's participations and description of the method of booking*

UniCredit Bank SA has no equity positions in the trading book as of 31 December 2016.

The Bank's strategy is focused on investments in companies which represent for UniCredit Group a long term development potential and with which mutual beneficial partnerships can be concluded, whereby the synergies of the partners can create value added for their shareholders.

The main participations as of 31 December 2016 are:

| Participation | Business Activity | Participation (%) |
|---|---|---|
| UniCredit Leasing Corporation IFN SA | Leasing | 99.98% |
| UniCredit Consumer Financing IFN SA | Financial services | 50.10% |
| Transfond SA | Financial services | 8.04% |
| Biroul de Credit SA | Financial services | 6.80% |
| Fondul Roman de Garantare a Creditelor pentru Intreprinzatorii Privati IFN SA | Financial services | 3.10% |
| Pioneer Asset Management S.A.I. SA | Financial services | 2.57% |
| Casa de Compensare Bucuresti SA | Financial services | 0.91% |
| **Visa Inc (USA) – preferred shares Series C** | Cards | 0.01% |

The total net book value of the participations as of 31 December 2016 is RON 163,396,202 out of which RON 143,115,683 represent investment in subsidiaries.

*See also Consolidated Financial Statements for 31.12.2016 - Note 24 and Note 25.UniCredit Bank SA has equity investments (shares) in unlisted entities whose fair value cannot be determined reliably, these participations are booked in the individual financial statements IFRS in accordance with the requirements in force, at cost.*

# 10. Interest rate risk on positions in the banking book

## *10.1. Scenarios used to measure and manage interest rate risk, quantification of the impact on the banking book of an interest rate shock*

Indicators to measure this risk are included in the risk profile.

Please see Market Risk chapter – the +/- 200 bp shock is run on the positions of the banking book separately and reported quarterly to the National Bank of Romania.

# 11. Financial Investment Risk

## *11.1. Description of Financial Investment Risk*

Financial Investment Risk is defined as the potential losses resulting from market value fluctuations of the Bank's own financial investment portfolio.

The strategy for the management of financial investment risk is performed by applying the following basic principles:

- The management of financial investment risk is performed though indicators and specific risk models like: impact on own funds, the market value of the participations, detailed figures within specific reports;
- Specific events will be considered within the stress scenarios.

# 12. Real Estate Risk

## *12.1. Description of Real Estate Risk*

Real Estate Investment Risk is defined as the potential losses resulting from market value fluctuations of the Bank's own real estate portfolios. This includes the portfolio of UCB, of the property ownership companies and its special purpose companies and shareholding companies. The real estate risk does consider the real estate property that is loan collateral.

The strategy for the management of real estate risk is performed by applying the following basic principles:

- The management of real estate risk is performed though indicators and specific risk models like: total real estate vs total assets, detailed figures within specific reports;
- Specific events will be considered within the stress scenarios.

# 13. Business Risk

## *13.1. Description of Business Risk*

Business Risk is defined as representing the adverse, unexpected changes in business volume and/or margins. It can lead to serious losses in earnings, thereby diminishing the market value of a company.

Business risk can result above all from: serious deterioration of the market environment, changes in the competitive situation or customer behaviour, as well as changes in the expense structure.

The Bank has implemented internal regulations and specific mechanisms in order to manage the Business Risk, and the capital requirements for this risk are included in the economic capital of the Bank.

UniCredit Bank

# 14. Strategic Risk

## 14.1. Description of Strategic Risk

The strategic risk is analyzed from the following perspectives:

- Risk of business changes;
- Risk of vicious implementation of the decisions;
- Risk of lack of reactivity;
- Regulatory risk.

The Bank implemented internal regulations and specific mechanisms in order to manage Strategic Risk.

# 15. Reputational Risk

## 15.1. Description of Reputational Risk

**Reputational risk** is the current or prospective risk to earnings and capital arising from adverse perception of the image of the financial institution on the part of customers, counterparties, shareholders/investors, regulators or employees (stakeholders).

Reputational risk can be triggered by negative publicity, true or not, relating to:

- Bank's reputation, respectively, the Bank's top management or their members
- The practices, tools, Bank liquidity or solvency

or

- Other risks arising in the Bank's activity, like for example being component of:
  - Operational risk (fraud, inadequate internal processes, failures of IT systems, security incidents, human errors etc);
  - Market risk;
  - Credit risk;
  - Liquidity risk.

Impact of reputational risk can affect the ability of the Bank to operate in accordance with the business plan, to establish new business relationships or continue existing partnerships with customers.

**Managing reputational risk**

The value system of UniCredit Bank is based on integrity as mechanism for conversion of profits into sustainable value, this implies a greater clarity to forward messages on relevant issues to employees, clients, financial community, regulators, nongovernmental organizations and general public. Thus, communication is a key factor in management of the reputational risk.

Bank's strategy, internal processes, important structural changes require special attention because of complex legal requirements, monitoring carried out by rating institutions and regulatory bodies and media interest.

Since each process/part of the banking activity may influence organization's reputation, the reputational risk management process will take into account:

- Each process / operations banking segment;
- Relationships with clients, especially in sensitive areas (confidentiality of information, respect for contracts, right to inform of clients, crisis management situations, the negative publicity, etc)

In crisis situation cases with impact in reputational risk occurrence (potentially negative situations), it is envisaged:

- Establishing communication strategy (defining transmitted and promoted key messages; defining channels for messages transmission)
- Sending messages through timely and brief press releases, updated when new elements appear (success of communication is assured by an adequate flow of information from the Management Board and the concerned business units towards Identity and Communication Department)
- informing call centers staff for determining patterns/responses to be answered in specific situations;
- Establishment of procedures and the competences for decisions making in case of crisis situations;
- Regularly updating web site or intranet of the Bank to ensure an adequate information flow.

Permanently, the Bank will try to limit the reputational risk by a transparent and efficient communication.

At UniCredit Group level, a set of policies regarding reputational risk were implemented. The purpose of these documents is to provide rules and principles for reputational risk assessment and management.

Considering the prevention pillar of reputational risk management, the Group developed Reputational Risk Special Policies defining principles and rules to consider and the flow to be followed for business with counterparties engaged in activities related to specific industries like: weapons/defence industry, nuclear energy industry, water infrastructure (dam) sector, mining industry, coal-fired power generation sector.

# 16. Excessive Leverage Risk

## *16.1. Description of Excessive Leverage Risk*

Risk of excessive leverage represents the risk resulting from the Bank's vulnerability due to leverage or contingent leverage that may require unintended corrective measures to its business plan, including distressed selling of assets which might result in losses or in valuation adjustments to its remaining assets.

The monitoring of risk of excessive leverage is realised based on specific instructions received from the Group and by taking into account the legal provisions in force.

Thus, the Leverage Ratio indicator, calculated according to instructions received from Group is included in the Risk Appetite Framework of the Bank. A system of limits comprising a Target level, a Trigger and a Limit is applied. Monitoring is done on a quarterly basis.

# 17. Liquidity risk

## *17.1. Liquidity*

The liquidity risk is defined as the risk that the Bank may not be able to fulfill its expected or unexpected financial obligations, without affecting its daily operations or its financial condition.

Among the main potential generators of liquidity risk, UniCredit Bank distinguishes between:

- **Liquidity Mismatch Risk/Refinancing Risk:** the risk of a mismatch between either the amounts and/or the timing of cash inflows and outflows;
- **Liquidity Contingency Risk**: the risk that future events may require a materially larger amount of liquidity than the bank currently requires. This might be due to the loss of liabilities, requirements to fund new assets, difficulty in selling liquid assets or difficulty obtaining needed new liabilities in the case of a liquidity crisis.
- **Market liquidity risk**: the risk that the institution cannot easily unwind or offset specific exposures, such as investments held as liquidity reserves, without incurring a loss because of inadequate market depth or market disruptions;

**Key Principles:**

Liquidity management is performed by UniCredit Bank in accordance with local binding laws and regulations and UniCredit Group Liquidity Management Framework. Clear and strict risk management principles are set according to the Bank's Risk Appetite Framework.

The main goal of Unicredit Bank's overall liquidity management is to keep the liquidity exposure at such a level that the Bank is able to honour its payment obligations on an on-going basis, but also during a crisis without jeopardizing its franchise value or its brand's name.

**Roles and Responsibilities**

A clear separation of duties and responsibilities is implemented in UniCredit Bank for an efficient and effective management of liquidity risk. Accordingly, the Bank keeps two governance layers:

- Managing Bodies acting as strategic decision-taking functions (as the Board of Directors, Supervisory Board, Assets and Liabilities Committee)
- Operational units acting as operative liquidity management functions, each being assigned different roles and responsibilities: ALM, Markets, Market Risk.

In particular, ALM provides strategic planning, management and supervision of the Bank's overall liquidity position, whilst Markets ensures operational short-term liquidity management (up to 1 year). Market Risk has the responsibilities of independent controls and reporting of liquidity risk.

**Risk Measurement and Reporting**

**Techniques for risk measurement**

Liquidity risk, for its particular nature, is addressed by means of gap analyses, liquidity stress testing, and complementary measures (mainly through a set of indicators: e.g. loan to deposit ratio, liquidity coverage ratio). This tools allow the measurement of liquidity risk over different time horizons and by currencies.

**Liquidity Framework**

UniCredit Bank's liquidity framework encompasses: short term liquidity risk mangagement (operational liquidity, up to 1Y) and structural liquidity risk management (liquidity position over 1y).

- **intraday liquidity management,**
  - The focus of intraday liquidity management is on actively managing the Bank's intraday liquidity obligations by timely meeting payments and keeping a sustainable intraday liquidity buffer.

- **Short-term liquidity risk management** (operational liquidity):

  Short term liquidity management and reporting focuses on the Bank's liquidity profile from 1 day up to one year.
  The aim of short term liquidity management is to maintain a sustainable equilibrium between cash inflows and cash outflows for the purpose of ensuring the normal operational continuity of the UniCredit bank's commercial business. The main activities for attaining such purpose are:
  - managing the access to the payment systems and of the cash payments (operational liquidity management)

- monitoring the level of the liquidity reserves and the extent of their utilization over time, with the objective of maintaining the liquidity reserves at appropriate levels in order to meet potential outflows.

As indicator of the short term liquidity risk, UniCredit Bank adopted the Operative Maturity Ladder (OML) by currency, whose main components are the net contractual cash flows (in/outflows) affecting the cash position of Bank, thus impacting directly the "core liquidity" of the bank over pre-defined time buckets, and the Counterbalacing capacity.

➢ **Medium and long-term liquidity risk management** (structural risk):

Structural liquidity management (over 1 year) aims at ensuring the financial stability of the balance sheet, with the objective of avoiding excessive and unexpected pressures on the funding requirements over the short term, whilst optimizing the funding sources and related costs. This is achieved maintenance of an adequate balance between the medium- long term and sticky assets and the respective stable sources of funding.

The main metric used to measure medium-long term liquidity risk is the Structural Ratio, which is calculated as the ratio between liabilities and assets with maturity above one year or more (i.e. contractual or modelled maturity, depending on their specific nature).

**Liquidity Stress Testing**

Stress testing is a risk management technique used to evaluate the potential effects on an institution's financial condition of a specific event and/or movement in a set of financial variables.

UniCredit Bank performs regular liquidity stress tests in order to diagnose the Bank's liquidity risk. The main scenarios of potential liquidity crisis identified are:

- Name Crisis - defined as a factual or market-hypothesized problem specific to the Bank, expected to cause a substantial reduction in counterparty limits by rating-sensitive costumers and inter-bank markets and possible withdrawal of Sight and Saving Deposits
- Market Downturn - defined as a generally negative development in the market's environment (e.g. broad sector, market or economic events) causing an increased stretch on available liquidity
- Combined - highlights the interconnections that stem from the happening of both economic turmoil and Bank's specific issues

In particular the results of the stress tests are useful for:

- o assessing the adequacy of liquidity limits

UniCredit Bank

- o assessing the right size of the counterbalancing capacity/liquidity buffer to withstand a given scenario within a defined timeframe
- o providing support to the development of the contingency plan.

**Monitoring and Reporting**

UniCredit Bank measures and manages liquidity based on monitoring system that envisages different types of restrictions – managerial and regulatory – embedded in risk metrics limits or warning/trigger levels.

In case of limit breach or warning level activation, Market Risk function investigates the rationale of the events, triggering the proper escalation and reporting them to the relevant committees.

**Risk Mitigation**

The main liquidity mitigation factors for UniCredit Bank are:

- planning and monitoring of the short-term and medium to long-term liquidity needs;
- an effective Contingency Liquidity Policy (CLP), including a Contingency Action Plan to be executed in case of market crisis
- a liquidity buffer to face unexpected outflows;
- liquidity stress testing performed on a regular basis.
- a system of early warning indicators to anticipate increased risk or vulnerabilities in the liquidity position or potential funding needs.

**Funding Plan**

The Funding Plan plays a fundamental role in overall liquidity management, influencing both the short term and long term liquidity position. It includes the set of the medium long term instruments (with relevant amount, maturity, timing, cost) to be realized in order to cover the expected funding deriving from the planned evolution of the liquidity uses and, avoiding pressure on the short term and ensuring complying with regulatory and managerial limits.

The Funding Plan is updated at least on a yearly basis and is aligned with the Financial Planning (Budgeting) process and the Risk Appetite Framework.

**Contingency Liquidity Management**

Contingency Liqudity Management has the objective of ensuring the availability of an effective organizational model in order to manage effectively the negative effects of a liquidity crisis situation, which is achieved through:

- setup of an extraordinary liquidity crisis governance model, linked to a set of early warning indicators, that can be activated in case of a crisis

- pre-definition of a set of available standby mitigating liquidity actions in order to be able to proceed timely
- consistent internal and external communicationcrisis.

A relevant part of the contingency liquidity management is the **Contingency Funding Plan**, which describes potential, but concrete actions the Bank can take in order to obtain additional funding in contingency situations and is complementary to the yearly Funding Plan. The measures foreseen are described in terms of a menu of actions together with sizes, instruments, and timing of execution aimed at improving the Bank's liquidity position during times of name or systemic crisis.

**Early warning indicators**

In order to identify emerging vulnerabilities in its liquidity risk position or potential funding needs, UniCredit Bank employs a set of early warning indicators linked to macroeconomic or market indicators and specific internal metrics. A specific activation mechanism is adopted in order to have sufficient time to inform senior management of a deteriorating situation situation and allow putting in place adequate actions aimed at restoring the business-as-usual state.

### *17.2. Funding (Asset Encumbrance)*

In accordance with the EU Regulation no.575/2013 as stipulated in the article 433 and EBA Guideline on disclosure of asset encumbrance (EBA/GL/2014/03), the Romanian UniCredit Group's encumbered and unencumbered assets, at consolidated level, for the year 2016 are disclosed using the EBA templates as stipulated in the above mentioned regulation.
The amounts are average values on quarterly basis for the year 2016.

**Template A - Assets**

Assets of the credit institution, split by type of assets stood at RON billion 34.61 *(as at 31.12.2016: RON billion 37.62).*

***- RON -***

| | 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, out of which: | 541,094,941 | | 34,072,541,476 | |
| Equity instruments | - | - | 27,310,292 | 27,310,292 |
| Debt securities | 537,455,121 | 537,455,121* | 5,812,947,753 | 5,812,947,753 |
| Other assets | 3,639,820 | | 1,465,401,952 | |

*Fair value of encumbered assets for the year ended 2016 (as presented in the Consolidated Financial Statement 31 December 2016) was RON 688,834,784.

During the year 2016, collateral received by the Romanian UniCredit Group amounted tp RON 59,207,639,002 and were not available for encumbrance.

**Template B – Collateral received**

*- RON -*

| | Fair value of encumbered collateral received or own debt securities issued | Fair value of encumbered collateral received or own debt securities issued available for encumbrance |
|---|---|---|
| **Collateral received by the reporting institution** | - | - |
| Equity instruments | - | - |
| Debt securities | - | - |
| Other collateral received | - | - |
| **Own debt securities issued other than own covered bonds or ABSs** | - | - |

**Template C - Encumbered assets/collateral received and associated liabilities**

*- RON -*

| | Matching lialibities, contingent liabilities or securities lent | Assets, collateral received or own debt securities issued other than covered bonds and ABSs encumbered |
|---|---|---|
| **Carrying amount of selected liabilities** | - | 541,094,941 |

**Template D – Narrative information**

The encumbered assets are approximate 1.56% of the Romanian UniCredit Group's total assets.

The Romanian UniCredit Group encumbered assets' portfolio and the sources of encumbrance includes:

- Government bonds placed as collateral in the clearing systems;
- Government bonds used by the Bank and its subsidiary UniCredit Leasing as guarantees for financing from the European Investment Bank.

In 2016, the Romanian UniCredit Group has increased its encumbered assets ( by approximately RON 180mn) as a result of UniCredit Group Romania's financing from European Investment Bank.

Bank's liabilities from the financing contract with the European Investment Bank should be covered at any time with eligible assets in the clearing system managed by Clearstream Banking SA Luxembourg. The collateral expressed as net market value of the accrued interest must be at least 103% applied to the maximum between the present value of the financing and the carrying amount of the financing.

Subsequent to the reporting period, the value of the assets encumbered has remained relatively constant.

The Romanian UniCredit Group' strategy for 2017 includes further increase of secured funding with probability of higher encumbered assets.

### *17.3. Liquidity Buffer and Funding strategy*

**Liquidity Buffer**

In order to avoid that short-term liquidity crunch or other unexpected events lead to potentially serious consequences, the Bank constantly maintains a liquidity reserve. This is a cushion represented by an ample amount of cash and other highly liquid assets to be promptly converted in cash (either through sale or collateralized funding) in case of ordinary or unexpected needs of liquidity, in accordance with regulatory and internal liquidity rules.

Stress testing (regulatory or internal stress scenarios) ensures that there is adequate liquidity both during normal economic cycles, as well as periods of sustained stress and that appropriate excess liquidity buffer is in place.

The major category in the Bank's liquidity buffer is represented by high quality bonds issued by the Government of Romania, eligible at Central Bank.

**Liquidity and Funding strategy**

UniCredit Bank reviews annualy its liquidity and funding strategy by considering the desired business model, the actual and expected macroeconomic/financial conditions and the funding capacity of the Bank, as well as the overall risk tolerance as reflected by the Risk Appetite Framework.

The strategic principle of "self-sufficiency" governs the liquidity and funding strategy of the Bank, which targets to achieve a well-diversified funding base, with priority given on the growth of local funding sources out of customer business with a variety of products (sight, savings, term deposits), as well as medium- and long-term placements of own issues. In accordance with this principle, the main strategic goals the liquidity and funding strategy encompasses are:

- optimization of the liquidity profile in line with liquidity limits in place and local regulatory framework
- self-sufficiency target fulfillment by achieving a sound commercial funding base and creating a foundation for full compliance with the relevant Risk Appetite Framework metrics

- achievement of main KPIs for each year in accordance with the Risk Appetite Framework, designed as quantitative targets defined in the yearly Funding Plan for, among others, the Liquidity Coverage Ratio and the Core Banking Book Funding Gap
- achievement of the necessary resilience towards stress scenario through building sufficient stock of the Counter Balancing Capacity, as targeted in the yearly Funding Plan
- exploring the advantage of cheaper sources like Covered Bond or Supranational Funding and evaluating the relevant maturities of medium/long term issuances
- keeping the funding dependency on short term wholesale external funding to a reasonable level necessary for reciprocity.

The main tool through which the Bank implements its liquidity and funding strategy is the Funding Plan. ALM is responsible for the execution of the Funding Plan, accessing the markets for medium and long term funding, in order to increase Bank's self-sufficiency, exploit market opportunities and optimize the cost of funds.

# 18. Remuneration Policy

## *18.1. Description of Remuneration Policy*

The Bank's remuneration policies are represented by the Human Resources Policy and the Rules on Remuneration – Compensation and Benefits.

The Bank's remuneration policies are approved by the Supervisory Board, upon the recommendation of the Remuneration Committee and are accessible to all employees. The Remuneration Committee has a consultative role and is responsible for preparing the decisions on remuneration topics that need to be taken

by the management body.

The Remuneration Committee of the Bank was set up by the Supervisory Board and is composed of 3 members chosen from amongst the members of the Supervisory Board. The Chairman of the Remuneration Committee is appointed by the Supervisory Board.

In 2016, the Remuneration Committee had the following composition:

- Mr. Carlo Vivaldi – Chairman
- Mr. Stefano Cotini – Member
- Mr. Heinz Meidlinger - Member

In the year 2016, the Remuneration Committee convened in six (6) ordinary and extraordinary sessions.

In accordance with the provisions of NBR Regulation nr. 5 / 2013, the remuneration practices for the members of the management body and identified staff are presented in a separate policy – i.e. Policy regarding the structure, composition, assessment of suitability and remuneration of management body and assessment of suitability for key function holders.

UniCredit ensures the alignment between remuneration and risk through policies that support risk management, rigorous governance processes based on informed decisions taken by corporate bodies and the definition of compensation plans that include the strategic risk appetite defined by the Risk Appetite Framework, the time horizon and the individual behaviors.

UniCredit uses a compensation mix formed of fixed and variable remuneration, as well as benefits.

The performance assessment process is subject to separate regulation setting out the steps of this process, the evaluation criteria and provides for a standardized framework for ongoing assessments.

According to the Rules on Remuneration – Compensation and Benefits:

Performance bonus award is approved by the management Board considering the following criteria:

- The financial performance of UniCredit Group
- The overall outcome of the whole group activity and of the bank considered
- The performance of the group / department the employee belongs to
- The sustainable individual performance of the employee

General rules for goal setting:

1. Part of the goals should contribute to the sustainability of results
2. Business performance criteria is risk adjusted
3. Individual criteria for performance assessment include competency assessment, respecting the values of the Group and the goals set
4. There is at least one indicator pertaining to Risk
5. There is a balance between financial and non financial goals

Economic goals must be avoided for Company Control Functions – Internal Audit, Risk Management and Compliance – and individual goals set for employees in these functions shall reflect primarily the performance of their own function and be independent of results of monitored areas.

Variable remuneration can be adjusted and reduced to zero (Malus) if the performance criteria at Group and Bank level are not fulfilled.

Performance remuneration will consider both individual and collective performance, thus settling both individual and collective objectives.

At individual level, evaluation criteria include qualitative and quantitative elements. Among the qualitative ones, there are included qualifications obtained by employee, compliance with systems and regulatory framework represented by the Bank's internal procedures, involvement in actions or significant projects and contribution to team's performance.

In addition to the above criteria, there are also used prudential criteria for risk adjustment, such as cost of capital and the income obtained after provisioning.

Remuneration package of persons with key management functions includes both fixed and variable elements, in order to achieve a balance and a motivation and retention tool:

- Fixed remuneration component compensates the role of the person and reflects the experience and skills needed for the respective position, as well as the demonstrated excellence level and overall contribution to the objectives of the organization.
- Variable remuneration component is designed to reward results and is correlated with both short-term goals and the long-term goals. Performance measurements consider both the overall performance of the Group and of the Bank, of the Business Area / Competence Line in which the person operates, as well as the individual sustainable results.

In accordance with NBR Regulation 5 / 2013 the variable remuneration offered to an employee will not be higher than 100% of the fixed total remuneration of each employee.

Remuneration policy and structure of compensation packages for persons with executive responsibilities are subject to annual approval of the Supervisory Board, based on the consultative opinion issued by the Remuneration Committee.

Supervisory Board ensures that remuneration policies are compliant to the culture, goals and long-term strategy of the bank and to its control environment, through the following actions:

- Approves remuneration policies
- Approves, after consultation with the Remuneration Committee constituted for this purpose, the remuneration practice for the Board members
- Approves the remuneration practices for the coordinators of the risk functions, for the directors of Internal Audit and Compliance departments

For the Management Board members, the performance measurement used to calculate the variable remuneration component includes an adjustment for all current and potential risk types and also considers the cost of capital and required liquidity.

For Management Board members, at least 50% of variable remuneration consists in non cash instruments and at least 40% of variable remuneration is deferred for a period of at least 3-5 years.

The Bank applies a performance adjustment practice, which enables the adjustment of the part (up to 100%) from an employee's bonus (Clawback) if:

- there is reasonable evidence that the employee participated in or was responsible for conduct which resulted in significant losses to the credit institution;
- there is reasonable evidence that the employee failed to meet appropriate standards of fitness and propriety;
- the Bank or the relevant operational unit suffers a material downturn in its financial performance; or
- the Bank or the relevant operational unit suffers a material failure of risk management.

UniCredit Bank

The remuneration policies and practices of the Group are also implemented at level of the directly controlled entities.

The bank did not have any employee who benefited from a total remuneration of at least 1 milion euro / financial year.

**Unicredit Bank – Quantitative Information**

| | | Members of the Management board | Investment banking | Retail Banking | Asset Mgmt. | Support functions | Independent Control functions | All other |
|---|---|---|---|---|---|---|---|---|
| Number of members of personnel | 0 | 5 | 2 | 7 | | 3 | 8 | 1 |
| Total number of full time employees | 0 | 7 | 36 | 2,032 | 8 | 265 | 227 | 342 |
| Total net profit (euro) | | | | | | | | 67,037,982 |
| Total remuneration (euro) | 0 | 2,542,832 | 1,988,986 | 31,736,695 | 249,550 | 7,269,528 | 6,083,274 | 5,048,827 |
| Of which total Variable Remuneration (euro) | 0 | 945,094 | 304,046 | 1,351,546 | 16,298 | 227,186 | 561,330 | 224,537 |

UniCredit Bank

Information about the remuneration for the management body and Identifies Staff for 2016 are presented in Annex 1.

| | Members of the management body in its Supervisory function | Members of the management Board | Investment banking | Retail banking | Asset management | Support functions | Independent control functions | All others |
|---|---|---|---|---|---|---|---|---|
| Number of personnel | - | 5 | 2 | 7 | - | 3 | 8 | 1 |
| Number of Identified Staff, in full time equivalent | - | 7 | 2 | 7 | - | 3 | 8 | 1 |
| Number of Identified Staff in senior management positions | - | 7 | - | - | - | - | - | - |
| Total fixed remuneration (euro) of which: | - | 1,597,738 | 193,362 | 699,933 | - | 190,962 | 528,790 | 62,221 |
| - cash | - | 1,597,738 | 193,362 | 699,933 | - | 190,962 | 528,790 | 62,221 |
| - shares and share-related instruments | - | - | - | - | - | - | - | - |
| - other instruments | - | - | - | - | - | - | - | - |
| Total variable remuneration (euro) of which: | - | 945,094 | 60,607 | 162,475 | - | 9,828 | 115,880 | 101,679 |
| - cash | - | 472,547 | 29,910 | 109,975 | - | 9,828 | 69,382 | 101,679 |
| - shares and share-related instruments | - | 472,547 | 30,697 | 52,500 | - | - | 46,498 | - |
| - other instruments | - | - | - | - | - | - | - | - |
| Total variable remuneration offered in 2016 and deferred (euro) of which: | - | 718,566 | 30,697 | 73,500 | - | - | 46,498 | - |
| - cash | - | 246,019 | - | 21,000 | - | - | - | - |
| - shares and share-related instruments | - | 472,547 | 30,697 | 52,500 | - | - | 46,498 | - |
| - other instruments | - | - | - | - | - | - | - | - |
| | | | | | | | | |
| Art. 450, (1) h), (iii) of EU Regulation n. 575/2013 - total amount of deferred variable remuneration, owed and unpaid, given in previous years and not in 2016 ( euro) | - | 1,410,791 | - | 159,017 | - | - | 48,350 | - |
| Total amount of explicit ex-post performance adjustments applied in 2016 for the remunerations confered in previous years (euro) | - | - | - | - | - | - | - | - |
| Total number of beneficiaries of guaranteed variable remuneration (sign-on bonus) | - | - | - | - | - | - | - | - |
| Total amount of guaranteed variable remuneration (sign-on bonus) in euro | - | - | - | - | - | - | - | - |
| Number of beneficiaries of severance payments | | | | | | | | |
| Total amount of severance given (euro) | - | - | - | - | - | - | - | 101,679 |
| Art. 450, (1), h), (vi) of EU Regulation n. 575/2013 - highest severance given to one person (euro) | - | | | | | | | |
| Number of beneficiaries of contributions to discretionary pension benefits in 2016 | - | - | - | - | - | - | - | - |
| Total amount of of contributions to discretionary pension benefits in 2016 (euro) | - | - | - | - | - | - | - | - |
| Total variable remuneration given over multiyear timeframes according to programs that are not revised annually (in euro) | - | - | - | - | - | - | - | - |

*See also Consolidated Financial Statements for 31.12.2016 - Note 12.*

## 19. Annex 1: Basel II Pillar 3 Disclosure for UniCredit Consumer Financing SA

### Chapter 1 – General requirements

#### 1.1 Strategy and general framework of risk management

UniCredit Consumer Financing (UCFIN) defines specific strategies and policies of risk management for the following types of risks, in a non-exhaustive manner:

1. Credit Risk
2. Market Risk
3. Liquidity Risk
4. Operational Risk
5. Reputation Risk

#### 1.2 Structure and organization of the risk management function

The risks control structure is based on several operational and control functions, defined as per the provisions of the Organizational and Functioning Regulation, as well as with the existent Group-level provisions.

**Supervisory Board (SB)**

The SB is responsible for the set up and keeping of a proper and effective internal control system.

In the context of internal control and significant risks management the Supervisory Board is responsible for the approval of the risk strategy. In connection with the strategic objectives of UCFIN, the Supervisory Board establishes a certain risk profile on an annual basis, the way to determine this profile and the frequency of monitoring.

**Management Board (MB)**

The Management Board is responsible to implement the strategy for defining the risk profile of the company, drafted by the Risk Division together with the GBS Division and approved by the Supervisory Board.

In this respect, the management implements/ensures: policies for measurement, monitoring and control of risk, reporting system for the measurement of exposures and of other aspects related to risks, in order to be reported to the proper management levels.

For the support of the risk management activities, specialised committees are set-up within the financial institution: Audit Committee, Risk Management Committee and Credit Committee.

UniCredit Bank

Audit Committee, according with the Internal Governance Manual of UCFIN and with its own rules of functioning, as approved by UCFIN, monitors the performance of the internal control system.

Risk Management Committee performs the activity related to risks identification, assessment and management according to the provisions of Organization and Operation Regulation of UCFin and to the provisions of its own approved regulation.

Risk Management Committee is a permanent organizational structure, constituted according to the legislation in force (NBR Regulation no 20/2009 regarding the non-banking financial institutions), having at least the following responsibilities, according to the NBR Regulation:

- to ensure the informing of Supervisory Board about the issues and the significant evolutions which may influence the non-banking financial institution results and its risk profile;
- to develop adequate procedures for the identification, evaluation, monitoring and control of the significant risks;
- to provide Supervisory Board sufficiently detailed and timely information, which will allow it to know and evaluate the management performance regarding the significant risks control and monitoring, according to the approved procedures, and the overview performance of the non-banking financial institution;
- to regularly inform Supervisory Board about the non-banking financial institution exposure to risks, and immediately if significant modifications are occurring in the current or future exposure of the institution to the identified risks.

**Risk and Collection**

It operates as a permanent organizational structure, with responsibilities related to the administration of the general framework of credit risk and operational risk management.

The Risk Division offers support to the Risk Management Committee and the company's management through the current monitoring of the credit risk and operational risk.

To ensure optimum management of credit and operational risk at a portfolio level and at individual level when the lending decision for each loan application, Risk Division is structured in 4 departments for risk management and monitoring. . Their responsibilities are detailed in the Company's Organization and Functioning Regulation:

- Decision – Risk Management Department
- Underwriting Department
- Collection Department
- Operational Risk&Fraud investigations

**Finance and Planning Area**

It offers support to the Risk Management Committee and the company's management through the current monitoring of the market and liquidity risk.

**Marketing and Product Development Department**

Marketing and Product Development Department offers support to Risk Management Committee and the company's management through the current monitoring of the reputation risk.

Operational risk is managed by all the departments whose activities incur operational risks. The monitoring is ensured by regular verification of the limits of operational risk indicators.

**Other organizational structures with responsibilities related to risk management**

Risk management function is supported at company level through other specialized committees (discipline committee, norms and procedures committee, projects committee, product and pricing committee, business continuity and crisis management committee, etc.).

**Chapter 2 – Own funds structure**

The structure of regulatory equity is detailed by own funds statement of the credit institution at each financial year end:

*- RON -*

| **Own Funds** | **31-Dec-16** |
|---|---|
| 1.1.1.1. Paid up capital | 209,169,548.00 |
| 1.1.1. Eligible Capital | 209,169,548.00 |
| 1.1.2.1.01.A. Legal reserve | **209,169,548.00** |
| 1.1.2.3.01 Audited profit – current year | 103,269,200.00 |
| 1.1.2. Eligible Reserve | 103,269,200.00 |
| 1.1.5.1. Intangible net assets | 105,051,576.00 |
| 1.1.5. Other deductions specific for Romania from own funds level I | 105,051,576.00 |
| 1.1. Own funds level I | 43,090,509.00 |
| 1.2.1. Basic Own funds level II | -43,090,509.00 |
| 1.2.2. Additional level II own funds, specific for Romania | 6,942,874.00 |
| 1.4. Total own funds level I | -6,094,102.00 |
| 1.5. Total own funds level II | -6,094,102.00 |

**Chapter 3 – Risk adjusted equity**

For the calculation of regulatory equity requirements in 2016, UCFin followed the requirements of Regulation No.20/13.10.2009. According to this Regulation non banking financial institutions must keep own funds at least at the level of minimum required subscribed capital and the aggregated eposure of the institution should not exceed 1500% of the own funds. Within UCFin the tasks related to the calculation and monitoring of needed capital are performed by the specialized departments of Financial and Risk areas.

For complying with capital adequacy requirements established by NBR Regulation No. 20/13.10.2009 and Group rules, UCFin is involved in a permanent evaluation process of capital requirements, for sustaining current and future activity, which implies the following processes:

1) Budgeting
2) Monitoring and analysis
3) Forecasting

**Quantitative informations**

- *RON* –

| Rows | Item | Label | Amount |
|---|---|---|---|
| 010 | 1 | TOTAL RISK EXPOSURE AMOUNT | **1,319,620,868.00** |
| 040 | 1.1 | RISK WEIGHTED EXPOSURE AMOUNTS FOR CREDIT, COUNTERPARTY CREDIT AND DILUTION RISKS AND FREE DELIVERIES | **1,319,620,868.00** |
| 050 | 1.1.1 | Standardised approach (SA) | **1,319,620,868.00** |
| 060 | 1.1.1.1 | SA exposure classes excluding securitisation positions | **1,319,620,868.00** |
| 070 | 1.1.1.1.01 | Central governments or central banks | 6,110,740.00 |
| 120 | 1.1.1.1.06 | Institutions | 45,411.00 |
| 140 | 1.1.1.1.08 | Retail | 1,265,673,848.00 |
| 160 | 1.1.1.1.10 | Exposures in default | 6,539,337.00 |
| 190 | 1.1.1.1.13 | Claims on institutions and corporates with a short-term credit assessment | 26,827,592.00 |
| 210 | 1.1.1.1.15 | Equity | 4,302.00 |
| 211 | 1.1.1.1.16 | Other items | 14,419,638.00 |
| **Capital Ratios** | | | |
| 010 | 1 | CET1 Capital ratio | 15.85% |
| 020 | 2 | Surplus(+)/Deficit(-) of CET1 capital | 149,786,608.94 |
| 030 | 3 | T1 Capital ratio | 15.85% |
| 040 | 4 | Surplus(+)/Deficit(-) of T1 capital | 129,992,295.92 |
| 050 | 5 | Total capital ratio | 15.85% |
| 060 | 6 | Surplus(+)/Deficit(-) of total capital | 103,599,878.56 |

UniCredit Bank

## Chapter 4 – Credit risk: general aspects

### 4.1 Assessment and identification of the credit risk

In determining the risk, the following elements are considered:

a) the current financial situation of the customers and their repayment capacity;
b) the exposures concentration over the counterparts and the economic areas
c) the capacity to apply, from legal point of view, the contractual commitments;
d) the financial commitments with persons having special relationship with the non-banking financial institution;
e) the purpose of the credit and the source of its repayment;
f) the debts service history for counterpart;
g) other specific characteristics of the customer and of the transaction that might affect the collection degree of the principal and the interests.

### 4.2 Credit risk management

The objective of credit risk management is to maximize profit by maintaining exposure to credit risk within acceptable limits.

The credit risk management is performed taking into consideration the credits both at individual level and at whole portfolio level and includes the consideration of the qualitative and quantitative aspects related to risks.

### 4.3 Principles and practices used in credit risk management

Credit risk management supposes a set of coherent principles and practices, oriented towards the following main directions:

a. Establishment of a framework and adequate parameters of credit risk;
b. Promotion and operation of a healthy and solid credit granting process;
c. Promotion and maintenance of an adequate process for credits administration, measurement and monitoring;
d. Permanent control over the quality of the loan portfolio.

Also, the credit risk management is performed depending on the stage of the credit granting process, as well as in the monitoring phase of the loans granted to customers, taking into account the development of the contractual relations.

UniCredit Bank

## Chapter 5 – Market Risk

**Market Risk** is defined as the risk of incurring losses due to unfavourable fluctuations of market prices (i.e. prices of shares, interest rates and exchange rates)

In case of UniCredit Consumer Financing, the market risk has the following two components:

- FX risk
- Interest rate risk

The main sources of the interest rate risk are: the poor correlation between maturity (for fix interest rate) and repricing date (for variable interest rate) for interest bearing assets and liabilities, negative evolution of the slope and the shape of the yield curve (unparalleled evolution of the interest rate performance of incomes generating assets and interest bearing liabilities), poor correlation regarding the adjustments of collected and paid instalments for different financial products having similar characteristics of interest reset.

The market risk management is performed through:

- identification, monitoring, analysis and control of market risks: FX risk, interest rate risk, according to group standards and NBR requirements;
- development and implementation of risk management strategy;
- reporting of market risk issues to the management of the Company.

The department responsible for monitoring market risk is UniCredit Bank's Market Risk Department.

The roles and responsibilities of market risk management are detailed in the Market Risk Rulebook for UCFIN.

## Chapter 6 – Liquidity Risk

**The liquidity risk** is the probability of the Company falling short of its due payments resulting from its contractual relations with costumers and third parties.

In case of UniCredit Consumer Financing, the liquidity risk has the following two components:

- the risk to not honour in time the obligations resulting from its contractual relations with customers and partners, or
- The risk to handle opportunity costs, in case the cash keeping is not too big and are not invested with bigger performance (in credit activity).

Liquidity risk management has to be done in conjunction with other significant risks, which may influence the liquidity position: credit risk, operational risk, reputation risk, interest rate risk, foreign exchange risk etc.

## Chapter 7 – Operational Risk

UniCredit Consumer Financing Operational Risk Management complies with legal and Group regulations in force, and it is performed according to the internal policies and procedures.

Operational Risk is considered a significant risk and is integrated into the UCFin's policy and strategy regarding significant risks.

Operational risk means the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events.

Operational risk includes legal risk, but excludes strategic and reputational risk. Legal risk includes, but is not limited to, exposure to fines, penalties, or punitive damages resulting from supervisory actions, as well as private settlements.

Operational risk events are those resulting from inadequate or failed internal processes, personnel and systems or from external or systemic events and other external events: internal or external fraud, employment practices and workplace safety, clients' claims, products distribution, fines and penalties due to regulation breaches, damage to Bank's physical assets, business disruption and system failures, process management.

Operational Risk Team is an independent function in charge with operational risk control, within the Risk and Collection Area and reporting directly to Chief Risk Officer (CRO).

The Operational Risk Team promotes the actions related to operational risk area and its responsibilities are:

- Manages the collection and validation of the operational risk events, analysing exposure to operational risk, examines scenarios, establish action plans based on the results of the operational risk indicators;
- Provides training and interact with all UCFin departments in order to achieve the above responsibilities;
- Monitoring the UCFin Operational risk exposure in accordance with the standards and policies defined at Group level;
- Control the quality of operational risk loss data and, periodically, provide data on operational risk (internal losses, risk indicators, scenario analysis, risk mitigation measures, reports to management);
- Provide support on risk appetite, budgeting and capital allocation, including operational risk mitigation costs;
- Propose operational risk mitigation plans, including insurance, and inform the relevant structures at the institution level;
- Assure, in collaboration with the Organization and Project Management Department, the implementation of mitigation actions proposed in the Permanent Working Group and escalates to the competent bodies, if case;
- Identify, in cooperation with relevant functions, operational risk indicators and scenario analyses, and ensure the quality of data collected, cooperate in analysing the impact of operational risk when introducing significant new products and significant changes in activities or organizational structure of UCFin;

- Verify and assure that the company has plans for business continuity in force and that they are regularly updated and tested.

The main instruments used for the management and control of operational risk in UniCredit Consumer Financing are internal operational risk events collection, monitoring of the operational risk indicators and operational risk reporting.

**Collection of operational risk internal events** is a main source for identification and quantification of operational risk. The process of collecting loss events is established through well defined rules for collection and validation of the data and for reconciliation of the loss data against the accounting bookings, in order to ensure completeness, accuracy and timeliness of data. The responsibilities regarding operational risk reporting are included also in the procedures specific to each area of activity.

The completeness and correctness of the operational risk database is ensured through the analysis of internal accounts, according to the process described in the Rules regarding reconciliation of accounting bookings against operational risk events.

At the institution level, there are implemented a number of **operational risk indicators.** The risk indicators are quantitative values that reflect the operational risk profile of a process or product. The value of an indicator should be correlated to changes in the level of risk. The process of monitoring the operational risk using indicators will help the responsible for operational risk management processes and responsibilities with:

- preventive control of the identified risk at the institution level (early signalling system risk);
- suggestions for risk mitigation and control;
- effective measures to reduce operational risk.

**Quarterly reports** regarding the exposure to operational risk, which analyse the aspects such as: financial losses detailed on event types, operational risk losses limit usage, capital requirement for operational risk, cross credit events, mitigation actions regarding operational risk are discussed in the Risk Management Committee. The reporting system includes at least bi-annual reports to the Supervisory Board.

The **capital requirement for operational risk** for UniCredit Consumer Financing is determined by the Group using the Basic Indicator Approach (BIA). The minimum capital requirement for operational risk according to BIA approach consist in applying a percent of 15% to the average of the relevant indicators of the last three ended financial years.

## Chapter 8 – Reputational Risk

### 8.1. Assessment and identification of reputational risk

Identification and assessment of reputational risk is performed at the overall level of Company and also at all organizational level of the Company and taking into account all the Company's activities, the outsourced activities, and the occurrence of some new activities.

From the point of view of reputational risk potential, a special attention must be granted to the following aspects:

1. Reaching or exceeding the limits established for the significant risks;
2. Reaching or exceeding some limits of the financial indicators (liquidity, solvability, etc);
3. Electronic mail – risk potential due to sending, by error or with intention, of some confidential/wrong information from the inside of Company to outside by e-mail, containing identification data from Company side;
4. External communication through unauthorized staff – risk potential by presenting partial data, personal points of view or breaking the confidentiality norms;
5. Staff fluctuations – pressure from the information confidentiality point of view, and also risk from procedures acquirement point of view regarding the Company's processes and especially of internal and external communication rules;
6. Negative media campaigns – risk potential by unilateral presentation of some aspects from Company's activity;
7. Focusing on specific sites of some opinion exclusive from unsatisfied customers, argued or not, aspects in question and notified to the responsible divisions/departments by the Company's staff;
8. Development of an adequate internal control system for supervising and performing of activities within the Society or for outsourced activities.

### 8.2. Reputational risk monitoring

The reputational risk monitoring is performed through:

- monitoring of all the publications related to UniCredit Consumer Financing;
- evaluation of articles which may represent a potential reputational risk for UniCredit Consumer Financing; establishment, together with the management of the communication strategy for each case;
- IT system monitoring and establishment of clear and restrictive procedures regarding the using ways of e-mail during the relation with the customers and in the external communication.

### 8.3. Management of the reputational risk

The general strategy in administrating this category of risk is realized, without being limited to this, at:

1. Applying a proper manner the internal norms regarding the know your customer policies and the regulations regarding anti money laundering.

2. Selection, through a rigorous analysis, of the clients that require credit facilities;
3. Elaboration of security politics/plans/measure for certain activities/services of the Company;
4. Adopting an adequate form of presentation/communication of informative materials and of the ones for the promotion of the activity and the products of the Company;
5. Establishing working instructions and competencies for decision taken in case of crisis situation;
6. Other measure for administration of reputational risks that the Society considers necessary;
7. Evaluation of the reputational risk, qualitative or quantitative (to be taken into consideration the losses produced by the negative publicity, litigations, etc.).

**8.4. Diminishing the reputational risk**

In crisis situations, with impact for the appearance of the reputational risk, the following aspects are to be considered:

- Establishing the communication strategy (definition of the key messages transmitted and promoted; definition of the channels used for communications);
- Messages transmitting through media communicates, briefly and promptly, periodically updated (the success of the communication is assured by an adequate information flow from the Management Board and the business departments involved);
- Trainings with the call centre personnel for establishing the methods/structures for answer providing, depending on specific cases;
- Establishing the procedures and competences of decision taking in case of crisis situation.

Usually, the Company will try to limit the reputational risk through procedures, rules and flows specially created in this respect and through a continuous and sustained communication, transparent and efficient.

For the administration and monitoring of the reputational risk all the departments within UCFin are responsible.

**Chapter 9 – Minimum capital requirement for credit risk**

UniCredit Consumer Financing, as part of UniCredit Group, established as strategic objective the maintenance in 2016 of a moderate risk profile. Even so, having in mind the present characteristics of the market and the financial crisis, it is possible that independently of the adopted measures, the limit set for the risk profile indicators to be exceeded. In this respect, the exceeding of the indicators of moderate risk is taken as trigger point.Thus, from the strategic point of view, the targeted risk profile for 2016 is a moderate risk, but the institution is prepared for a medium risk profile, reaching this limit not being an objective by itself.

*Required capital for coverage of unexpected losses*

According to the Strategy for management of significant risks in UniCredit Consumer Financing, the institution must calculate the capital requirements for covering the significant risks.Normally, this required capital (economic capital) is different from the minimum capital calculated according to the regulations in force regarding capital adequacy.

For local consolidation purposes, the economic capital for UCFin, calculated through the Financial Investment Risk method is received from the Group twice a year. The method is applied for "small legal entities" and covers all significant risks (credit, operational and market).

**Chapter 10 – Credit Risk Mitigation Techniques**

The Company diminishes the credit risk through:

✓ granting credit exposures towards counterparties with performing rating;

✓ the customer rating is periodically reviewed, at least annually;

✓ for concentration risk limitation, thresholds on exposures on certain industries, regions, financing currencies, categories of debtors and rating are set;

✓ the credit granting and valuation of credit risk process is periodically reviewed with the aim of its adequacy to the size and complexity of the activity, to the development strategy, etc. and, not least, to the legal regulations in force;

✓ detailed analysis on the entire loan portfolio is periodically performed;

✓ identification of the credits to be valuated in view of calculating provisions on individual basis and segmentation of the credit portfolio on buckets with similar credit risk characteristics for the analysis and valuation on collective basis;

✓ judgments on the quality of the credit risk of the credit portfolio takes into consideration relevant internal and external factors that might affect the collection level of the credits (such as political, geographical, economical and industrial factors);

✓ implementing a systemic and logical method of consolidating the estimated losses and ensuring that the registered provisions are aligned with the applicable accountancy environment and with the relevant prudential regulations;

Considering the development of the Company's activity and the modifications registered in the general strategy, the limits regarding credit risk are reviewed and modified whenever necessary, in order for an adequate correlation to be reached between the Company's risk profile and the targeted profitability

A well-structured segregation of duties is considered in order to ensure that responsibilities that might drive to conflicts of interests are to be allocated to different departments/divisions.

The Company has IT systems due to which the credit risk issues are reported on time (for instance: monthly close monitoring of the credit portfolio can help identify certain risk concentrations).

A rating system or scoring is used in credit risk valuation, system that facilitates the analysis of the information and elements presented in the financial documents of the customer (private individual).

With the aim of preventing the losses due to non-payment within a credit transaction, UCFin monitors the fulfilment of the client's obligations through:

- ✓ constant monitoring of the turnover through the customer's accounts – this must be relevant in relation with the granted loan amount;
- ✓ constant monitoring of the fulfilling of the credit contract stipulations (including the conditions);
- ✓ classification and allocation of loan loss provisions;

If deviations from the contractual conditions or deterioration of the customers' financial situation and/or solvency are identified, the Company must come with a written proposal to the customer in order for him to take some specific steps to eliminate the reasons of the deviations.

The Company accepts exposures from the credits granted to private individuals differentiated according to the customer's associated risk and to the type of transaction/product. The correlation of the credit risk classes with rating classes is established through internal specific procedures regarding the provisions calculation and determination.As the credit activity is permanently growing, the credit portfolio structure might suffer modifications, considering the Company's development strategy.The departments responsible for identification, assessment, management and monitoring of the credit risk are the following: departments within the Risk and Collection Division, Operations Department, IT&C Department and Accounting Department.

# 20. Annex 2: Basel II Pillar 3 Disclosure for UniCredit Leasing IFN

### 1 – General requirements

### 1.1. Strategy and general framework of risk management

Unicredit Leasing Corporation IFN S.A. defines its strategies and general framework for the following risk types, without being restrictive: credit risk, market risk, liquidity risk, real estate risk, operational risk, reputational risk, financial investment risk, business risk.

### 1.2. Structure and organization of the risk management function

The risk control structure is based on a multitude of operational and control functions, defined in accordance with the Regulation of Organization and Operation of UniCredit Leasing Corporation IFN SA (UCLC), but also with the rules existing at group level.

Some organizational structures are:

- *The Supervisory Board (SB)* is responsible for the set up and keeping of a proper and effective internal control system.
- *The Board of Directors* is responsible for implementing the strategy and the policies on risk management.
- *Risk Management Committee* - is a strategic committee and has the responsibility of identification, evaluation and management of significant risks and has to meet at least quarterly or any time when required. This committee has the following main responsibilities:
    - Consultancy and advisory functions,
    - Decision functions
    - Information and reporting functions (including reports to be presented to the UCLC Supervisory Board)
- *Audit Committee* is responsible to assist the Company's Board in defining and preparing the principles and guidelines governing the entity's entire internal control system, on the basis of a risk-oriented approach, and assessing its effectiveness and efficiency, so that the main risks are properly identified, then measured, managed and monitored, subject to the Board's responsibility for all decisions on this matter.
- *Credit Committee* – has responsibilities of approval of the new transactions and credit reviews as per competences framework in order to assure the required quality of the portfolio and to limit the credit risk as required by the credit policies.
- *Special Credit Committee* - is responsible for approval of restructured cases, IFRS provisioning level for individually assessed clients, according to competencies and specific Regulation.

- *Permanent Workgroup Committee for Operational Risks* is responsible for operational risk identification, mitigation actions proposed and monitoring of the mitigation actions in place.

***Credit Operations Division (CRO)***

CRO Division works like a permanent organizational structure, with reponsabilities related to management of the general framework of risk management.CRO division supports the Risk Management Committee and the Board of Directors through significant risks management monitoring systems.

**Significant risks management activity** is achieved through dedicated departments within the Credit Operations Division, as follows:

- Financial Analysis & Approval (Underwriting Department)
- Risk Strategies and Control Team
    - Risk Strategies and portfolio management
    - Risk Control
- Collection & Restructuring Department
- Financed Asset Management Department (both, financed and repossessed assets).

**2 – Own funds structure**

The structure of regulatory capital is detailed by own funds statement of the credit institution at the end of the financial year 31.12.2016:

- *RON* -

| Elements taken into account | No. row | Amount |
|---|---|---|
| Subscribed capital paid / endowment capital | 1 | 90,989,013 |
| Premium related to capital | 2 | 13,663,461 |
| Legal reserve | 3 | 13,493,733 |
| Statutory or contractual reserves | 4 | - |
| Other reserves from net profit | 5 | 8,366,409 |
| Net profit carried forward | 6 | 40,622,497 |
| Interim net profit recorded until determination of own funds, net of any foreseeable liabilities and verified by the individuals involved in the field of non-bank financial institutions, according to the accounting and valuation principles and rules in force | 7 | - |
| **Total (row 1 to row. 7)** | **8** | **167,135,113** |
| The amounts of net profit of the previous financial year consisting in dividends | 9 | - |
| Loss carried forward | 10 | - |
| Current financial year result representing loss | 11 | - |
| Profit appropriation | 12 | 4,015,366 |
| Depreciated value of set-up costs | 13 | - |
| Depreciated value of other intangible assets | 14 | 5,361,357 |

| | | |
|---|---|---|
| Depreciated value of goodwill | 15 | - |
| Value of intangible assets in progress and advances granted for intangible assets | 16 | - |
| Own shares repurchased to reduce capital | 17 | - |
| Value of transactions on terms of favour (if applicable) | 18 | - |
| **Total (row 9 to row. 18)** | **19** | **9,376,723** |
| **Equity (row 8 - row 19)** | **20** | **157,758,390** |
| Reserves and special funds created under special regulations | 21 | - |
| Reserves from revaluation of tangible assets and other revaluations according to the law | 22 | 336,502.00 |
| Subordinated loans received, including funds made available to non-bank financial institutions, treated by law as subordinated loans | 23 | 99,904,200 |
| Other elements of nature of funds and / or stocks that meet the requirements of Art. 62, para. (2) of Regulation *) | 24 | - |
| **Additional capital (total row. 21 to row. 24)** | **25** | **100,240,702** |
| Amounts representing interests in other entities, which exceed 10% of the share capital of the latter, subordinated loans and other receivables of a similar nature to those entities | 26 | 44,182,887 |
| **Own funds (row 20 + row 25 - row 26)** | **27** | **213,816,205** |

### 3 – Risk capital adequacy

For the calculation of regulatory capital, UCLC applied during 2016 the requirements of Regulation No. 20/13.10.2009 reviewed. According to this Regulation the non-banking financial institutions must keep own funds at least at the level of minimum required subscribed capital and the aggregated exposure of the institution should not exceed 1500% of the own funds. In order to calculate the regulatory capital, UCLC used during the year 2016 the approach imposed by local regulations (NBR) for credit risk.

Within UCLC, the tasks related to the calculation and monitoring of needed capital are performed by the specialized departments of Financial Division and CRO Division.

For complying with capital adequacy requirements established by Regulation No. 20/13.10.2009 and Group rules, UCLC is involved in a permanent evaluation process of capital requirements, for sustaining current and future activity, which implies the following processes:

4) Budgeting
5) Monitoring and analysis
6) Forecasting

For the **budgeting** process:

- The different business segments provide the budgeted volumes for the following year;
- Risk Strategies and Control department estimates the credit risk provisions based on the above volumes;
- Strategic Planning and Control Department calculates the capital requirement and compares it with the existing capital;
- In order to assure an adequate level of capitalization, RWA optimization actions are considered. Starting from the capitalization objectives, UCLC establishes measures for optimizing the structure of its loans and guarantees.

**Monitoring and analysis** process implies:

- Monthly calculation of capital requirement;
- RWA optimization actions;
- Optimal capital allocation in order to add value to the shareholders.

**Forecasting process:**

- During the entire year, several forecasting actions are performed in order to have estimations as accurate as possible of the capital requirement evolution.

## 4 – Credit risk: general aspects

***Assessment, identification and credit risk management***

UCLC is exposed mainly to credit risk in financing activities. Credit risk is the most important type of risk the company is facing. Thus, the most important risk generating activity is financing, but any other activity of the company may be generating potential credit risk (extra balance sheet commitments).

The following types of risks are considered components of credit risk in our company:

A. The risk of default;
B. The concentration risk;
C. The residual risk.

Credit risk management involves a set of principles and practices oriented towards the following directions:

1. Establishing an adequate framework and parameters for credit.
2. Promote and operate a healthy and robust process to grant funding.
3. Promoting and maintaining an adequate management, measurement and monitoring financing process
4. Providing a permanent control on loan portfolio.

***Specific procedures for credit risk management and mitigation***

Policies and procedures related to lending and credit risk are established and implemented according to assigned roles and responsibilities so as to ensure the following:

- maintaining healthy financing standards;
- monitoring and controlling credit risk;
- identifying and managing non-performing loans.

The entities involved in financing and monitoring activities ensure credit risk management both at each financing level and on an aggregate level across the whole portfolio, credit risk elements are analyzed in correlation with other risk types that are in a close relationship of interdependence, considering the following main coordinates:

- concentration risk;
- default risk.

Measures taken by UCLC in the direction of credit risk mitigation are focused on:

- assessing the debtors' reimbursement capacity at individual level;
- establishing specific credit risk provisions to absorb expected losses;
- avoiding concentration of loans on: sectors, categories of debtors, financing products;
- spreading the credit risk by diversifying customer database and product types financed;
- consulting credit risk information - CRC;
- consulting information regarding payments incidents, using Unicredit Bank resources;
- monitoring the exposure undertaken by the company from "a single debtor" and / or persons in special relationship, to which UCLC has large exposures;
- monitoring the quality of the database from the company computer system;
- monitoring the performance of the company customers' portfolio;
- periodically reviewing the customer's analysis system (scoring system);

Also, UCLC uses credit risk mitigation techniques through specific activities and procedures that monitor the default risk and the concentration risk.

***Treatment and valuation of credit risk***

For a prudential valuation of the credit exposures, there were implemented rating systems based on which the exposures are classified considering the related credit risk assessment for each debtor, through a general scale of default risk assessment.

Internal ratings and default probability plays an essential role in the entire credit risk management process within UCLC.

Rating valuation is an important part of the credit approval process. Credit risk tolerance takes into consideration credit granting limitation based on rating classes. Thus, there will be no credit granting to the clients with a non-performing rating (according to internal classification).
Later on, during the credit tenor, the rating information is an important part of monitoring as well as of restructuring and of the progress of the non-performing credits.
Risk reporting and portfolio management framework is focused on the rating information (coming to complete the information of the debt service).
The ratings and the respective probabilities of default represent the base element of the IFRS provisions methodology for companies.

***Determination of value adjustments/ provisions***

***Approaches and methods applied for the calculation of NBR value adjustments***

In order to cover potential credit and investment losses, the company calculates value adjustments according to the NBR regulations in force.
Consequently, for the determination of the adjustments value level, the credit exposures are classified based on the following elements:

- ✓ obligor performance category;
- ✓ delinquency (number of overdue days);
- ✓ initiation of judicial procedures.

The financial performance reflects the economic potential and financial strengthens of an obligor, determined based on the analysis of a set of qualitative and quantitative factors.

**Approaches and methods applied for the calculation of value adjustments - for the credit portfolio under the Standardized Approach**

Provisions represent the loss amount estimated by the company based on impairment models. The company uses two approaches for this estimation:

- Individual assessment
- Collective assessment

Through **collective assessment**, the provisions are calculated on a portfolio level basis by dividing it into similar credit risk characteristics buckets. The performing portfolio is subject of collective assessment entirely, no matter if the exposures are considered significant or not.

The non-performing portfolio is subject of collective assessment only in the in case the exposures are not considered significant.

Through **individual assessment**, the provisions are individually calculated for each individually significant exposure. Individual assessment is a process of measurement of exposure impairment for an individual client.

The individual assessment process has been divided into 2 steps:

- Identification of individually significant exposures and/or exposures of clients which may be individually assessed
- Individual loss estimation for provisioning purpose for the respective exposures.

**5 – Market Risk**

**Market Risk** is defined as risk of registering losses or non achievement of expected profits, which appears at as a consequence of prices, interest rate and exchange rate fluctuations.

In case of UCLC, the market risk has the following two components:

- Foreign exchange risk (FX)
- Interest rate risk

Market risk is monitored through quarterly analysis by the Planning Department together with the Treasury Team. Second level control activity is provided by Risk Strategies and Control Team. The analysis is made on interest type and currency type but also on each maturity in order to find the gaps between assets (portfolio) and liabilities (refinancing) with regards to the above mentioned factors that could influence market risk. All data presented in the quarterly market risk report are verified and reconciled with balance sheet data sent by the Finance Department. The data are being analysed by Management and by Unicredit Bank and Market Risk measures are proposed and also taken in order to reduce the gaps between financing and refinancing with regards to interest types, currency types and also maturity classes.

The main sources of risk associated with interest rate is poor correlation between the maturity (for fixed interest rates) or the date of re-pricing (for floating interest rate) for interest bearing assets and liabilities, the negative evolution of the slope and shape of the yield curve (evolution of interest rate yields unparalleled income generating assets and interest bearing liabilities).

Market Risk management is achieved through specific procedures and techniques, based on continuous monitoring and analysis of several indicators.

Currencies and interest rate positions monitoring is conducted by Treasury Team with Risk Strategies and Control Team, and monitoring has been done by Market Risk department of UniCredit Bank.

**6 – Liquidity Risk**

Liquidity risk reflects the possibility that UCLC can have difficulties in making expected or unexpected cash payments when due, thus affecting daily operations or financial condition of the company.

Liquidity risk is managed by Finance Department, Treasury Team which reports to the Chief Financial Officer (CFO) and is managed on a consolidated basis as defined by Group Policy liquidity. Second level control activity is provided by Risk Strategies and Control Team.

In the liquidity risk, the following risks are taken into account:

- discrepancies in liquidity risk
- market liquidity risk
- refinancing risk

UCLC makes a clear distinction between short-term liquidity management (day-to-day management) and the management of medium and long term financing needs, avoiding the possible liquidity problems.

To manage short term liquidity risk, the company monitors the daily cash flow forecasts compared with the total liquidity position and the position of the exchange rate. UniCredit Group supports the company with necessary funds for refinancing and flexible repayment terms, so the risks of liquidity in all other forms are eliminated.

The company uses as an alternative to the refinancing obtained from UniCredit group, long-term cooperation with several international financial institutions. Monitoring of liquidity limits has been done by Market Risk department of UniCredit Bank.

**7 – Real Estate Risk**

The real estate risk is caused by the potential losses resulting from market value fluctuations for the company's real estate assets: offices / buildings owned directly or recovered, when the collection process is completed.

Reporting process for real estate risk is subject to the UniCredit Group Policy "Pillar II - Methodological Manual on Internal Capital" along with further instructions received from the Group (Risk Integration and Control Team), and is made by Risk Strategies and Control Team, from Credit Operations Department - CRO line.

Real estate risk is monitored quarterly by analyzing the existence or absence of each and every case of real estate risk:

- Directly owned real estate assets (not part of the leasing contract) are checked, along with the Finance Department (CFO line) to see if any new acquisitions of real estate assets have been made during the last quarter;

- Recovered assets (if the contract is closed and the collection and legal proceedings have been concluded) are checked with Collection and Restructuring Department (CRO line) to see if there is any case of repossessed real estate assets during the last quarter.

**8 – Operational Risk**

Operational risk exposure of UCLC results from the possibility of occurrence of operational risk events due to inadequate or failed internal processes, personnel and systems or from external or systemic events (which impact the whole financial system): internal or external fraud, employment practices and workplace safety, clients claims, fines and penalties due to regulation breaches, damage to company's physical assets, business disruption and system failures, process management.

Identification and collection of operational risk losses is based on the following categories:

1. **Internal frauds** – losses resulting from actions intended to defraud, misappropriate property of goods (in legal way) or circumvent regulations, the law or Company's policy, involving at least one party inside the Company and excluding malicious damage. The internal fraud is originated inside the Company and the internal nature of the event must be definitely ascertained, otherwise it should be considered as external fraud.
2. **External frauds** – losses resulting from actions intended to defraud, misappropriate property or circumvent the law committed by a third party, without the assistance of an employee and excluding malicious damage.
3. **Employment relationship and safety at work** - losses from violating employment or health or safety laws and agreements, personal injury claims or diversity discrimination events/practices.
4. **Clients, products and business practices** - unintentional or negligent failure to meet obligations to clients (including fiduciary and suitability requirements) or from the features of a product. The events where the Company committed an improper business act fall into this category, likewise when it has been the victim of similar practices by other Company.
5. **Damage to physical assets** - losses resulting from deterioration of physical assets, caused by natural disaster or other similar event type.
6. **Business disruption and system failures** are losses arising from interruptions or inadequate functioning of systems.
7. **Execution, delivery and process management** are failed transactions processing or process management, or losses coming from relations with counterparties and vendors. These events are not intentional and involve documenting or completing business transactions.

**Scenario analysis** has the role to evaluate the company's exposure to operational risk in case of low frequency and high impact events. Scenarios are used in order to evaluate the risk of internal processes taking into account not only the historical losses, but also the potential losses.

**Operational risk indicators** reflect the operational risk profile and are correlated to changes in the risk level. Monitoring operational risk indicators represents an early warning system for changes in the operational risk exposure and it is conducted on a monthly basis by the Risk Strategies and Control Dep. The indicators and their thresholds are reviewed at least annually or when changes occur in their composition.

The strategic objective in terms of operational risk is to significantly reduce losses due to the production of operational risk, respectively losses due to inadequate internal processes, human error and errors of various automated systems and those due to factors external to the company.

Risk Strategies and Control department in Credit Operations Division interact with all departments in order to collect and validate data, operational risk exposure analysis, for scenario analysis, defining action plans and monitoring operational risk indicators.

**9 – Reputational Risk**

Reputational risk refers to the potential risk to profits and capital arising from negative perception of the image of UCLC from customers, third parties, shareholders, investors or regulators. This impact could affect the company's ability to establish new business relationships or continue existing partnerships with customers. Reputational risk is defined by the possibility of negative publicity (media), true or not, regarding company practices could cause a decrease in the customer database, sales revenue and / or costly actions in court.

From the point of view of reputational risk potential, a special attention must be granted to the following aspects:

- Reaching or exceeding the limits established for the significant risks;
- Reaching or exceeding some limits of the financial indicators (liquidity, solvability, etc);
- Electronic mail – risk potential due to sending, by error or with intention, of some confidential/wrong information from the inside of Company to outside by e-mail, containing identification data from Company side;
- External communication through unauthorized staff – risk potential by presenting partial data, personal points of view or breaking the confidentiality norms;
- Staff fluctuations – pressure from the information confidentiality point of view, and also risk from procedures acquirement point of view regarding the Company's processes and especially of internal and external communication rules;
- Negative media campaigns – risk potential by unilateral presentation of some aspects from Company's activity;
- Focusing on specific sites of some opinion exclusive from unsatisfied customers, argued or not, aspects in question and notified to the responsible divisions/departments by the Company's staff;

Reputational risk management is carried out through:

- Appropriate application of KYC (know-your-customer) rules and regulations in force relating to the prevention and combating money laundering

- Selecting customers who request financing, through a rigorous analysis,
- Adequate training of staff in charge with customer relationship management, including topics related to banking secrecy;
- Taking appropriate measures to manage and mitigate the extension of negative consequences by the internal structure within which the reputational risk generating element appears
- Development of appropriate forms of presentation / communication and information materials to promote the company's activities.
- Reputational risk assessment may be qualitative or quantitative (taking into consideration: the number of suspected money laundering cases reported to the authorities, the number of new disputes in a period that can generate losses for the company, the number of customer complaints and resolved customer complaints in favour of the customer in a period etc.).

A specific compliance activity does not eliminate reputational risk, but reduces the frequency and severity of incidents as well as the severity of reactions from regulatory bodies.

**10 – Financial Investment Risk**

Financial Investment Risk is defined as the potential losses resulting from market value fluctuations of equity holdings. Financial Investment Risk is defined as follows.

1. Market or Book Value of equity holdings;
2. Volatilities and correlations of the relevant stock price or market indices.

Financial Investment Risk can be measured under two points of view consistently with different goals:

1. retrospective for monitoring purposes;
2. forward-looking for capital planning purposes within the budget;

For monitoring purposes, Financial Investment risk is measured on a quarterly basis by CFO line.

**11 – Business Risk**

Business risk is defined as adverse, unexpected changes in business volume and/or margins. It can lead to serious losses in earnings, thereby diminishing the market value of a company.
Business risk can result above all from:

1. serious deterioration of the market environment;
2. changes in the competitive situation or customer behavior.

Because of its nature, the business risk cannot be subject to mitigating actions, given that most of the key underlying drivers (e.g. regulatory changes, competitive changes, etc.) could suffer from external impacts with effects that could not be properly or entirely mitigated in advance by managerial actions. Although, the company is continuously trying to diversify the range of products offered, to monitor and reduce if the case, the limits on industries that are facing difficulties.