

CONSOLIDATED

DATED

BANCA
S I S T E M A
CONTEMPORARY BANK

FINANCIAL

STATEMENTS

AS AT

31 DECEMBER

2016

Group Banca SISTEMA

**CONSOLIDATED FINANCIAL
STATEMENTS**

AS AT 31 DECEMBER 2016

BANCA
S I S T E M A

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CONSOLIDATED REPORT ON
OPERATIONS AS AT 31 DECEMBER 2016

COMPOSITION OF THE PARENT COMPANY'S MANAGEMENT BODIES

Board of Directors

Chairman	Ms	Luitgard Spögler
Deputy Chairperson	Prof.	Giovanni Puglisi
CEO and General Manager	Mr	Gianluca Garbi
Directors	Mr	Claudio Pugelli
	Prof.	Giorgio Barba Navaretti (<i>Independent</i>)
	Ms	Ilaria Bennati (<i>Independent</i>)
	Mr	Daniele Pittatore (<i>Independent</i>)
	Ms	Carlotta De Franceschi (<i>Independent</i>)
	Mr	Andrea Zappia (<i>Independent</i>)

Board of Statutory Auditors

Chairman	Mr	Diego De Francesco
Standing Auditors	Mr	Biagio Verde
	Mr	Massimo Conigliaro
Alternate Auditors	Mr	Gaetano Salvioli
	Mr	Marco Armarolli

Internal Control and Risk Management Committee

Chairman	Mr	Daniele Pittatore
Members	Ms	Carlotta De Franceschi
	Prof.	Giorgio Barba Navaretti
	Ms	Luitgard Spögler

Nominations Committee

Chairman	Mr	Andrea Zappia
Members	Ms	Ilaria Bennati
	Ms	Luitgard Spögler

Remuneration Committee

Chairman	Prof.	Giorgio Barba Navaretti
Members	Mr	Andrea Zappia
	Prof.	Giovanni Puglisi

Ethics Committee

Chairman	Prof.	Giovanni Puglisi
Members	Ms	Ilaria Bennati
	Mr	Marco Pompeo

Surveillance Body

Chairman	Mr	Diego De Francesco
Members	Mr	Daniele Pittatore
	Mr	Franco Pozzi

The Board of Directors was appointed by resolution of the Shareholders' Meeting dated 27 November 2015, with the appointment of Ms Luitgard Spögler to the position of Chairman of the Board of Directors. Subsequently, the Board of Directors, meeting on the same date, appointed Mr Gianluca Garbi to the position of CEO and set up the Executive Committee, the Internal Control and Risk Management Committee, the Nominations Committee, the Remuneration Committee, the Ethics Committee and the Surveillance Body. Following the resignation of Mr Michele Calzolari, tendered on 31 May 2016, on 10 June 2016 the Board of Directors co-opted Ms Ilaria Bennati as Director. In addition, the abolition of the Executive Committee became effective on 4 July 2016, with the resulting reorganisation of the Board committees, and Mr Giovanni Puglisi was appointed Deputy Chairperson. The Board of Statutory Auditors was appointed by resolution of the Shareholders' Meeting dated 22 April 2014.

HIGHLIGHTS DATA AS AT 31 DECEMBER 2016

Balance Sheet Data (€,'000)

Total Assets		1,999,363	-17.1%	31 Dec 16
		2,411,670		
Securities Portfolio		514,838	-44.4%	31 Dec 15
		925,402		
Loans - Factoring		986,169	-6.1%	
		1,049,832		
Loans - Salary-backed loans and SME		344,911	69.5%	
		203,466		
Funding - Banks and REPOs		753,706	-40.7%	
		1,271,164		
Funding - Term Deposits		443,395	-22.5%	
		572,379		
Funding - Current Accounts		436,986	30.2%	
		335,541		

Profit and Loss Data (€,'000)

Interest Margin		71,000	22.4%
		58,006	
Net fee and commission income		9,060	-18.9%
		11,168	
Operating Income		81,483	13.5%
		71,814	
Personnel Expenses (*)		(15,169)	15.5%
		(13,139)	
Other administrative expenses (*)		(20,907)	4.0%
		(20,112)	
Profit before Taxes (*)		37,334	9.4%
		34,139	

Performance Indicators

Cost/income Ratio (*)		45%
		46%
ROAE (**)		25%
		34%

(*) Amounts and indicators were calculated using profit and loss data adjusted for non-recurrent costs.

(**) The Return on Average Equity (ROAE) was calculated as the ratio of the profit for the year to average shareholders' equity.

SIGNIFICANT EVENTS DURING THE REPORTING PERIOD

The Board of Directors approved the following on 5 February 2016: (I) the Activity Plan for 2016 related to the II Level Internal Control Functions, (Risk, Compliance and Anti-Money laundering) and Internal Audit Department, and (II) the Board of Directors' Regulations. The Board of Directors also acknowledged the quarterly report from the Internal Control Department as at 31 December 2015 (Risk Reporting, Tableau de bord of the Compliance Department and Tableau de bord of the Internal Audit Department), as well as the quarterly report on Transactions with Associated Parties within the scope of the Master Resolution. In addition, the Board of Directors, upon confirmation of the decision made on 16 December 2015 regarding the purchase of a building for the Bank's new headquarters, approved the establishment of a new, wholly owned vehicle (a limited liability company) with a view to further developing the business. This company will deal with property asset management, in addition to other activities (e.g. the management and sale of advertising space, cultural and educational events, etc.), possibly even on behalf of third parties.

On 15 March 2016 the Board of Directors approved: (I) the 'Annual report on the procedures for providing services, investment activities, ancillary services and activities related to the distribution of financial products issued by insurance companies and banks as per CONSOB decision no. 17297', (II) the '2015 Risks Department Annual Report', (III) the '2015 Compliance Department Annual Report', (IV) the '2015 Anti-Money Laundering Department Annual Report', (v) the 'Compliance Department Annual Report on complaints received by the Bank', (VI) the 'Annual Report on the activities carried out by the Internal Audit Department during 2015', and (VII) the Periodic Report to the Board of Directors and Board of Statutory Auditors from the Surveillance Body concerning the application of the 'Organisation, management and control model pursuant to Legislative Decree 231/2001". The Board of Directors also approved the Report on corporate governance and ownership structure which was prepared in accordance with art. 123-bis of Legislative Decree no. 58/1998, as

well as the updated IT System documentation (IT Security Policy, IT Risk Summary Report, Information Technology and Communication Adequacy and Cost Summary Report). Following the resolutions dated 16 December 2015 approving the Remuneration Policies of the Banca Sistema Group for 2016 and the launch of the 2016-2019 Stock Grant Plan with approval of the relevant Regulation, as well as the ensuing resolutions for the creation of a legal reserve of profits linked to the free share capital increase reserved to beneficiaries of the 2016-2019 Stock Grant Plan and the free share capital increase pursuant to article 2349 of the Italian Civil Code servicing the Stock Grant Plan, following approval of the proposed amendment of article 5 of the Articles of Association, on 24 March 2016 the Board of Directors approved some changes to the previously approved versions that it deemed necessary based on indications received from the Supervisory Authorities.

On 25 March 2016, the Bank of Italy issued the authorisation provision - pursuant to Articles 77 and 78 of Regulation (EU) no. 575/2013, as well as Article 29 of Commission Delegated Regulation no. 241/2014 - for the repurchase of the Common Equity Tier 1 capital instruments issued by the Bank as resolved by the Shareholders' Meeting on 27 November 2015 for a predetermined amount not exceeding €1,477,649.49 (amount to be deducted entirely from own funds as of the authorisation date) for the following purposes: (I) to support regular trading performance so as to avoid price movements that are not in line with the market movements and to guarantee market making (Article 29 (3) of Commission Delegated Regulation no. 241/2014); (II) to pay a portion of the variable remuneration in shares to key personnel as set out in the remuneration and incentive policies approved by the Shareholders' Meeting (Article 29 (4) of Commission Delegated Regulation no. 241/2014); (III) provide the directors with a flexible, strategic and operational tool that will allow them to use own shares as consideration for any extraordinary transactions, such as acquisitions or investment exchanges, with other parties regarding transactions of interest to the Bank. The maximum amount

available for this purpose is €140,000 (Article 29 (5) of Commission Delegated Regulation no. 241/2014);

On 28 April 2016, the ordinary and extraordinary Shareholders' Meeting decided on the following:

- 1) the approval of the financial statements of Banca Sistema S.p.A. as at and for the year ended 31 December 2015;
- 2) the allocation of the profit for 2015, with the payment of a dividend of €0.053 per share;
- 3) the approval of the 2016 Remuneration Policies of the Banca Sistema S.p.A. Group, with a maximum limit of the ratio of the variable component to the fixed component of remuneration of 2:1 for positions falling into the category of "key personnel";
- 4) to acknowledge the Remuneration Report, drafted in accordance with Part One, Title IV, Chapter 2, of Bank of Italy Circular no. 285 of 17 December 2013, approved by the Board of Directors on 24 March 2016, with a favourable opinion on Section I;
- 5) to approve the 2016 Stock Grant Plan, concerning the free assignment to beneficiaries of ordinary shares of the Company at the end of the first cycle of the 2016 Plan, contingent on the achievement of certain company and individual performance targets;
- 6) the establishment of a specific restricted equity reserve in service of the 2016 Stock Grant Plan and the 2017-2019 plans that may in future be approved by the Shareholders' Meeting in respect of the years of accrual 2017, 2018 and 2019, designated the "Restricted reserve for capital increase in service of stock-grant plans for bonuses in 2016, 2017, 2018 and 2019", in the amount of €1,600,000.00, to be drawn from a pre-existing free equity reserve consisting of "undistributed profits" identified in the "Undistributed profit reserve";
- 7) to approve (according to the authorisation received from the Bank of Italy on 26 April 2016 by provision no. 552423) a free share capital increase, pursuant to Article 2349 of the Italian Civil Code and Article 5.4 of the Articles of Association, in

divisible form, in service of the 2016 Stock Grant Plan, and in service of the stock grant plans that may in future be approved by the Shareholders' Meeting in respect of the years of accrual 2017, 2018 and 2019. The maximum amount of this free share capital increase is a nominal €49,920, corresponding to a maximum number of 416,000 ordinary Company shares with a par value of €0.12 each, and it must be executed by 30 June 2023. The free share capital increase will involve the use of the restricted reserve for share capital increases in service of the 2016 Plan and the 2017-2019 Plans (established in the amount of €1,600,000).

Within the framework of the securitisation transaction approved by the Board of Directors on 5 February 2016, on 4 March 2016 an agreement was signed to sell the first portfolio of receivables relating to salary- and pension-backed loans to the special purpose vehicle Quinto Sistema Sec. 2016 S.r.l. for a book value of €119.6 million, with the subsequent issue of ABS on 29 March 2016. The SPV Quinto Sistema Sec. 2016 S.r.l. was included in the list of SPVs under no. 35253.4 on 9 March 2016. On 24 March, the bond documents for the issue of the ABS were signed, while the OTC repo contract (structured as a sale and repurchase agreement) was signed on 29 March. Finally, on 30 March the settlement transactions for both the issue of the ABS (subscribed by Banca Sistema) and the Repo contract regarding the senior tranche were concluded. The amount of the issue was €120.9 million. On 23 May a new portfolio of salary-backed loans was sold to the SPV Quinto Sistema Sec. 2016 for a book value of €24.1 million partly financed through collection of principal from the securitised portfolio (€1.8 million), with the remainder funded through further payments "called up" on the ABS according to their "partly paid" structure. Following the second sale, the total securitised portfolio reached an outstanding value of approximately €138 million. On 23 May, the OTC repo contract was renewed for a term of two months in the case of the senior tranche for an amount (following the sale of the new portfolio) of €111.9 million (rolling over the initial repo, which had a nominal value of €93.5 million) refinanced, as in the case of the previous

transaction, without a haircut at an annual interest rate of 0.503% (including commissions).

On 29 April 2016, the Board of Directors, as part of a larger process of revising the Bank's organisational structure, approved (I) the abolition of the Executive Committee, (II) the resulting revision of operating powers and (III) the reorganisation of the compositions of the Board committees, in addition to the appointment of the new Deputy Chairperson of the Board of Directors (Mr Giovanni Antonino Puglisi) and the new Compliance Officer (Ms Daniela Mosconi). Furthermore, the Board of Directors also approved the reorganisation of the company structures through (I) the establishment of the new Collection Department, which will be responsible for management and recovery of the receivables of the Bank and third parties, and (II) the merger of the Central Factoring Department and the Central Banking Department to form the new Central Commercial Department. All of the above changes became effective on 4 July, following the expiry of the period of five business days from 24 June 2016, the date the Bank of Italy issued the provision authorising the purchase by Banca Sistema S.p.A. of a 100% equity interest in Beta Stepstone S.p.A..

In addition, the Board of Directors approved the update to the Liquidity Policy and Contingency Funding Plan, the 2015 ICAAP Report, the 'Annual report from the Internal Audit Department concerning audits conducted on the outsourced operating functions' and the Regulations for the Coordination of the Internal Control Department. Furthermore, the Board acknowledged the quarterly report by the Internal Control Department as at 31.3.2016 (Risk Reporting, Tableau de Bord of the Compliance Department and Tableau de Bord of the Internal Audit Department), the quarterly report on Transactions with Associated Parties within the scope of the Master Resolution and the Pillar III Disclosure.

Banca Sistema's first senior bond issue, approved during the session of the Board of Directors held on 29 April, was concluded on 3 May 2016. The placement in a club deal reserved for institutional investors, in the total amount of €70 million has a term of two years, with a fixed rate and an all-inclusive cost of 200 bps. The issue is part of a plan to diversify the forms of funding, in accordance with

the Funding Plan, and allows for improved asset liability management.

Following the resolutions passed by the Board of Directors on 16 December 2015 and 5 February 2016, on 21 April 2016 a preliminary purchase agreement was signed for the purchase of a building which will also serve as the Bank's new headquarters.

On 10 June 2016, the Board of Directors approved Banca Sistema's participation in the second plan of targeted long-term refinancing operations ("TLTRO-II") for a maximum available amount of €123 million. Based on the bids received, Banca Sistema subscribed the operation for the maximum amount available (€ 122,850,000.00). The operation was allotted on 24 June 2016 with spot settlement on 29 June 2016. The Board of Directors also approved the Regulations of the Internal Audit Department. In the context of a new securitisation transaction approved by the Board of Directors on 10 June 2016, the following sales contracts were signed on 30 June: the Sales Contract (including the Guarantees), Servicing Contract and Corporate Servicing Contract (for the management of the SPV). The portfolio of loans sold includes 145 enforceable injunctions amounting to total principal of €23.9 million, with €7.7 million of accrued late payment interest (of which €1.5 million relating to repaid capital invoices and €6.2 million of invoices that have yet to be repaid).

On 21 June 2016 Banca Sistema and the majority shareholders signed an agreement with Axactor AB, a company listed on the Oslo Stock Exchange, for the acquisition of a 90% equity interest in CS Union S.p.A., an Italian company active in the field of debt recovery and the purchase of non-performing loans (NPLs). The transaction was finalised on 28 June, with the sale to Axactor of the 15.8% equity interest in CS Union held by Banca Sistema, which will therefore continue to hold a 10% interest in the company, for a pre-tax capital gain of €2.3 million in the first half of 2016. The consideration (€3.8 million) was settled 60% in cash and the remainder in shares of Axactor. A three-year shareholders' agreement was also signed by Banca Sistema and Axactor for the joint development of the NPL business in Italy.

After having signed an agreement with Stepstone Financial Holdings on 4 February 2016 for the acquisition of a 100%

interest in Beta Stepstone S.p.A. and having received notice of authorisation from the Bank of Italy on 24 June 2016, on 1 July 2016 the acquisition was finalised for consideration of €57.2 million. The acquisition price includes a share of late payment interest not yet collected by Beta of approximately €16.3 million; an identical amount was paid as a security deposit and will be released to the seller only after the collection of the aforementioned late payment interest. The consideration was also adjusted based on shareholders' equity at the closing of the transaction (30 June 2016), which will result in an adjustment in favour of Banca Sistema of €633 thousand. The purchase is in line with the strategic plan of Banca Sistema as notified in July 2015 during the IPO. The purchase strengthens the Bank's presence in the factoring market for healthcare operators in Central and Southern Italy.

The following measures became effective on 4 July 2016, in accordance with the resolutions passed by the Board of Directors on 29 April 2016:

- the abolition of the Executive Committee, with the resulting expansion/update of the powers previously granted to the CEO and General Manager;
- the reorganisation of the composition of Board committees;
- the reorganisation of company structures through the establishment of the new Collection Department and the merger of the Central Factoring Department and Central Banking Department into the Central Commercial Department.

On 29 July 2016, the Board of Directors approved the plan for the merger by incorporation of Beta Stepstone S.p.A. into Banca Sistema S.p.A.. The application for authorisation of the merger pursuant to art. 57, paragraph 1, of the Consolidated Law on Banking was therefore submitted to the Bank of Italy on the same date.

On the same date, the Board of Directors also acknowledged the quarterly report by the Internal Control Department as at 30.6.2016 (Risk Reporting, Tableau de Bord of the Compliance Department and Tableau de Bord of the Internal Audit Department), as well as the quarterly report on Transactions with Associated Parties within the scope of the Master Resolution, for which the update was approved

and the due date set for July 2017.

The vehicle Largo Augusto Servizi e Sviluppato S.r.l. (LASS), fully owned by Banca Sistema, with capital of €4 million, was incorporated on 25 August 2016. The company's purpose includes, among others, the promotion of and participation in real-estate investment transactions, primarily with companies belonging to the banking group. On 31 August 2016, LASS then purchased a property located at Largo Augusto 1 in Milan, Italy, for a total of €21.5 million, which will also be used as the Bank's new headquarters, once the planned restructuring work has been completed.

On 21 September 2016, the Board of Directors acknowledged the "Periodic Report to the Board of Directors and Board of Statutory Auditors from the Surveillance Body concerning the application of the 'Organisation, Management and Control Model pursuant to Legislative Decree 231/2001".

On 10 October 2016, authorisation was received from the Bank of Italy pursuant to art. 57 of the Consolidated Law on Banking for the merger by incorporation of Beta Stepstone S.p.A. into Banca Sistema. On 15 November 2016, the Board of Directors then decided on the merger which was then finalised on 12 December 2016. The merger became effective beginning on 1 January 2017.

On 18 October 2016, the Bank of Italy commenced the inspections regarding the "governance, management and control of credit risk". Then on 22 November 2016, the scope of the inspections being made by the Bank was broadened, upon the request of CONSOB, to include aspects related to investment services provided by the Bank and to the status of companies listed on the stock exchange.

On 19 October 2016, ratings were assigned to the securitisation of the portfolio of salary- and pension-backed loans (CQS and CQP), which has a total value of €170 million. Moody's and DBRS assigned the senior class (€133 million) ratings of Aa2 and A, respectively, and the mezzanine class (€16 million) ratings of A3 and BBB, respectively. Those securities will be listed on the Luxembourg Stock Exchange. The junior class of €21 million is unrated.

The senior notes, to date used by Banca Sistema for

refinancing operations with institutional investors, will thus be eligible for refinancing operations with the ECB.

The deal is in line with the strategy to diversify funding sources and will enable the Bank to pursue its growth targets in this business segment.

On 28 October 2016, the Board of Directors resolved to approve the start of a new business, effective as of 1 December 2016, in the collateralised loans sector, pursuant to art. 48 of the Consolidated Law on Banking, and the opening of a new branch in Milan, on via Vespri Siciliani, to be dedicated exclusively to this activity. The branch will begin operating in the first quarter of 2017.

On the same date, the Board of Directors also resolved to launch a self-assessment process of the Corporate Bodies which was completed during the meeting on 15 December 2016 with the approval of the “Board of Directors Self-Assessment Document” and the document on the “Optimal qualitative and quantitative composition

of the Board of Directors”.

Always on 28 October 2016, the Board of Directors also acknowledged the quarterly report by the Internal Control Department as at 30.9.2016 (Risk Reporting, Tableau de Bord of the Compliance Department and Tableau de Bord of the Internal Audit Department) and verified that the independent directors continue to meet the independence requirements.

On 15 December 2016, the Board of Directors approved certain changes to the Bank’s organisational structure. Among these that are worthy of mention, the Head of the Compliance and Anti-Money Laundering Function will report directly to the Board of Directors and the Underwriting Department will be separated from the Finance and Administration Department through the creation of a new Department that reports directly to the General Manager and CEO. These changes became effective beginning on 1 January 2017.

THE MACROECONOMIC SCENARIO

The last quarter of 2016 was influenced by one significant event for the world economy: the presidential elections in the United States. On 8 November 2016, the citizens of the United States elected the Republican Party candidate and entrepreneur, Donald Trump, as President.

Even though the global economic conditions improved slightly in the last quarter of 2016, this event caused considerable uncertainty. If on the one hand the budget policies announced by the new administration might encourage an expansionary impact, on the other hand, the spread of restrictive trade measures could have unfavourable results and lead to turbulence in emerging economies.

The global growth outlook is improving but is affected by uncertainty in economic policies. China reported modest economic growth in the last quarter of 2016, recovering from the slowdown of the previous months, although the risks tied to private sector and local government indebtedness still persist. Advanced economies recorded a slight expansion in trade in 2016, encouraging growth in global trade, albeit at a rate that was below estimates. The same could not be said for emerging economies, which recorded a sharp slowdown. Oil prices are increasing thanks to a new agreement to cut production. However, this increase may not have a lasting effect partly because of the geopolitical tensions in the main production areas, and also for a possible upturn in US production, which could lead to a decrease in global demand. In general, both emerging and advanced economies have adopted expansive monetary policies.

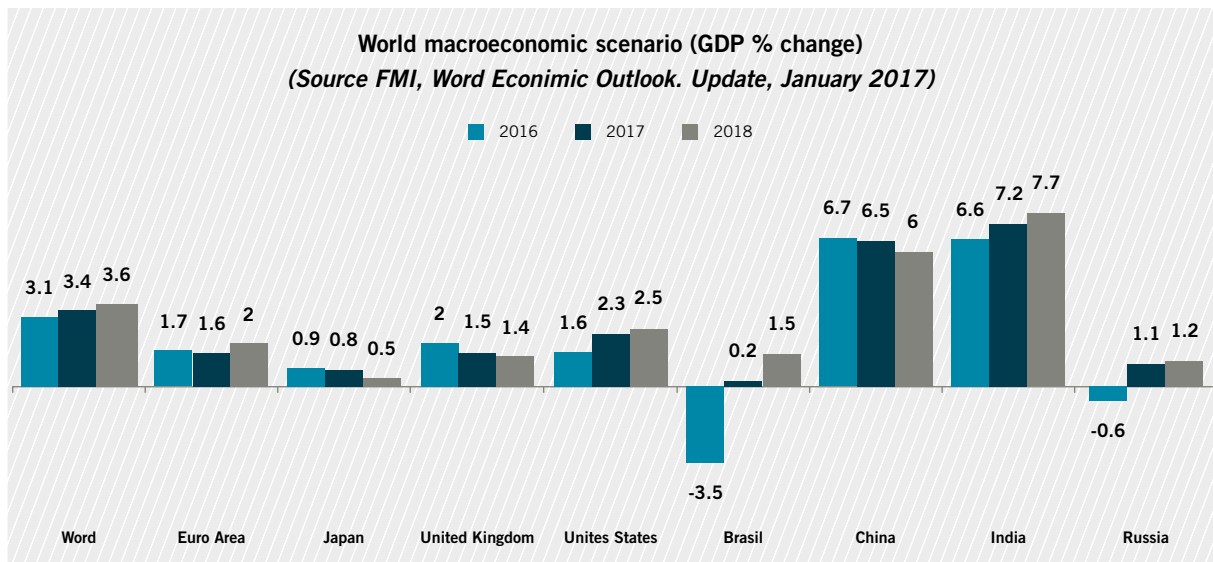
Growth continues in the Euro area: as reported in Economic Bulletin no. 1 2017 of the Bank of Italy, issued on 13 January 2017, in the third quarter of 2016 GDP increased by 0.3% driven by domestic demand

components. The reasons for this faster growth are to be sought in increased household spending, public consumptions and the change in inventories.

According to the Bulletin estimates, also the last quarter was influenced by a growth rate just over the previous period. In December, the €-coin indicator prepared by the Bank of Italy, which measures the underlying performance of the area's GDP, increased yet again, confirming that economic activity is expanding.

Inflation is also rising and was 1.1% in December compared to 0.6% in November. This, however, was thanks to the acceleration in prices for fresh food and energy. Therefore, excluding volatile factors, base inflation remains stable. In order to monitor the inflation trend to guarantee that monetary conditions ensure it increases, at the meeting on 8 December, the ECB Governing Council extended the duration of the Eurosystem asset acquisition programme until prices have stabilised.

The ECB continues to closely monitor the financial markets in order to prioritise contacts with other central banks and is ready to provide additional liquidity, if needed. To guarantee this, the ECB introduced four new targeted refinancing operations with longer terms of four years and highly advantageous conditions. The third operation was launched on 21 December, with the aim of stimulating the supply of credit and supporting economic activity and price performance in a number of channels. In the last quarter of 2016, both loans to businesses and households increased thanks to the stabilisation of the average financing cost to the lowest level recorded since the start of the Monetary Union (about 1.8%). Following the US presidential elections, capital outflows in emerging countries resumed along with a depreciation in currencies and an increase in exchange rate volatility.



ITALY

The modest recovery continues thanks to the increase in household spending and investments.

In the third quarter of 2016, as highlighted in the Bank of Italy's Economic Bulletin, GDP increased by 0.3%, which is in line with European trend, and continued to increase, albeit at a slower pace, in the last quarter of 2016.

Industrial activity continued to expand favouring a stabilisation of the real estate sector even though uncertainty increased in the non-residential sector. Manufacturing and retail trade activity improved in the third quarter of 2016 while the construction sector worsened.

Business confidence indicators remained quite high, albeit with uneven performances in the major sectors of the economy, and above all in the foreign component.

The outlook for investment spending is improving and is estimated to increase again in 2017 thanks to new incentives for investments in technology assets and an extension in those intended to reduce the cost of capital. Expectations regarding inflation have also increased, guaranteeing additional support to the willingness to invest.

In addition, in the third quarter of 2016 the net bond funding of Italian companies was positive.

Household consumption continues to strengthen, although at a slower pace than the previous period. The willingness to save has progressively increased

even though it remained at a moderate level. Disposable income also increased during 2016 (about 2.3% compared to the previous period), thanks to improvements in employment. Spending on durable and semi-durable goods slowed, while the purchase of non-durable goods and services increased.

Italian household debt continued to decrease in proportion to disposable income (61.4%), remaining below the average for the euro area (95% at the end of June). Interest rates on new loans decreased further. In the third quarter of 2016, exports of goods and services remained stable compared to the previous period. Exports of services increased by 1.3%.

Imports also decreased (0.7% by volume), but at a slower pace. The current account surplus continued to improve, rising to €40.4 billion in the first eleven months of 2016 (nearly double that of the same period of the previous year), thanks above all to the strong performance of the trade surplus, due to the decreased expenditure on energy products.

Foreign purchases of Italian government bonds decreased compared to the previous period, especially due to a gradual rebalancing of resident household portfolios towards insurance and managed savings products. Investments in foreign securities by Italian residents continued to increase.

Employment increased, both fixed term and permanent, while the growth in labour cost was zero.

Loans to the private sector grew at a moderate pace. Loans to households increased, while loans to businesses differ by economic sector: loans to manufacturing and constructions companies decreased while loans to service companies continue to increase.

The funding of Italian banks remains substantially stable. Credit quality continues to improve, while remaining high. Overall economic activity may continue

to strengthen thanks to the accommodating monetary policy and the gradual strengthening in lending.

The risk for the recovery of the global economy arises from the possible implementation of protectionist policies and the turbulence that may arise from the new US president, and in the uncertainty in negotiations to establish the new trade relations between the European Union and the United Kingdom after Brexit.

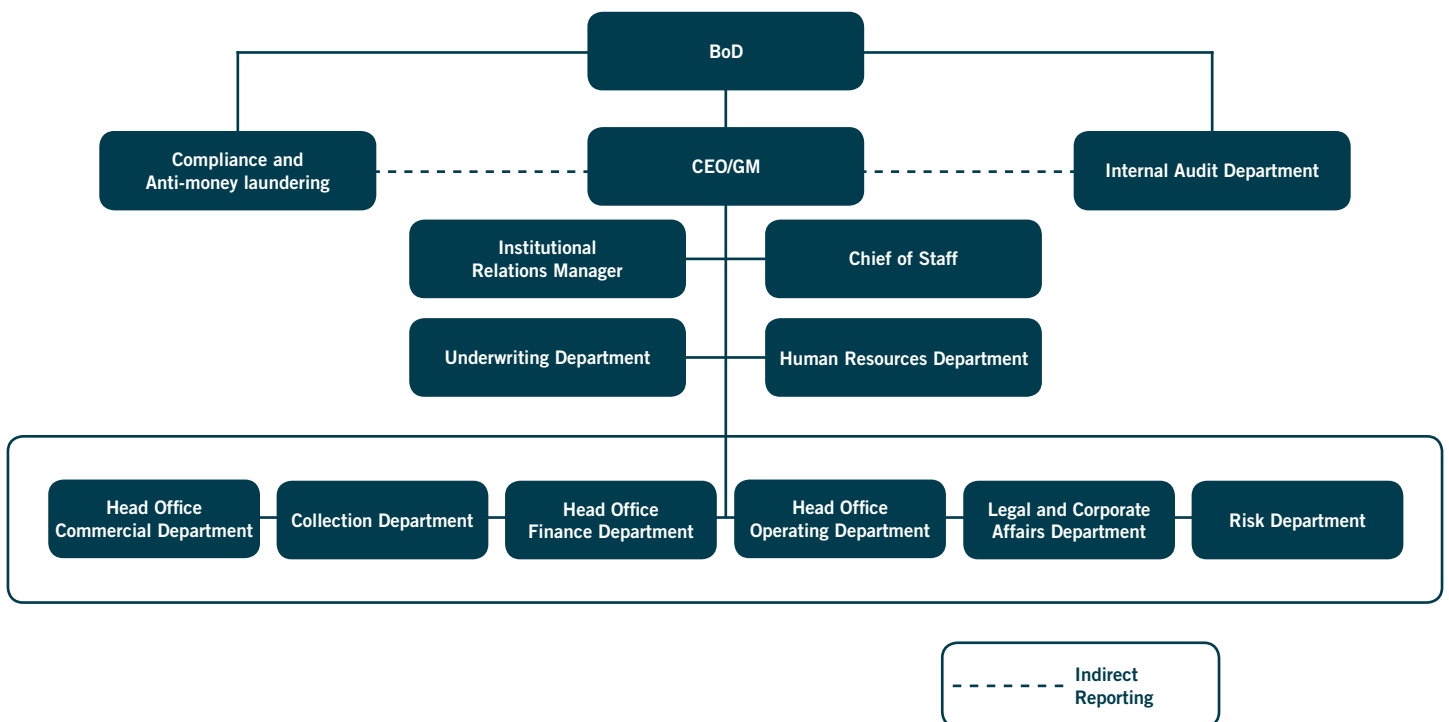
COMPOSITION AND ORGANISATIONAL STRUCTURE OF THE GROUP

Scope of the banking group

On 31 December 2016, the Banca Sistema Group comprised the Parent Company, Banca Sistema S.p.A., and Specialty Finance Trust Holdings Limited, a company incorporated under the laws of England, and Beta Stepstone S.p.A. (incorporated into the Bank beginning on 1 January 2017) and Largo Augusto Servizi e Sviluppo S.r.l. (incorporated on 25 August 2016), both of which are fully owned by the Bank.

Organisational chart

An updated organisational chart of the Parent Company, Banca Sistema, is shown below:



GENERAL MANAGEMENT

The following report to the CEO and General Manager:

- Central Commercial Manager
- Central Financial Manager
- Collection Manager
- Risk Manager
- Central Operating Manager
- Legal and Company Affairs Manager
- Underwriting Manager
- Human Resources Manager
- Chief of Staff
- Institutional Relations Manager

REGISTERED OFFICES AND BRANCHES OF THE BANCA SISTEMA GROUP

The Registered Offices and Branches of the Banca Sistema Group are as follows:

- Milan - Corso Monforte, 20 (Registered office and branch)
- Rome - Piazzale delle Belle Arti, 8 (Administrative office)
- Pisa - Galleria Chiti,1 (branch)
- Padua - Via Savonarola, 217 (Administrative office)
- Palermo - Via della Libertà, 52 (Administrative office)
- Naples - Via Toledo, 156 (Legal and administrative office)
- Watford - (UK) CP House, Otterspool Way (Representative Office)

HUMAN RESOURCES

As at 31 December 2016, the Group had a staff of 144, broken down by category as follows:

FTEs	31/12/2016	31/12/2015
Senior managers	19	15
Middle managers (QD3 and QD4)	43	33
Other personnel	82	82
Total	144	130

On 31 December 2016, the headcount included 14 new resources attributable to the new Beta Stepstone subsidiary. Considering these new hires, the number of resources remains unchanged with a total of 24 new resources added during the year in the Banking, Collection and Reconciliation areas, the Beta subsidiary,

and the Director Middle Office, and an equal number of leavers, 24; of these, 3 were employees of SF Trust Holding.

The average age of Group employees is 40 for men and 38 for women, with women accounting for 41% of the total.

The Italian factoring market

The market situation, as previously highlighted in the first half of 2016, is characterised by overall growth of the sector that exceeds the forecasts published by the most important specialised observers. Data from Assifact in November 2016 shows operator turnover up 8% on the same period in 2015. Preliminary sector turnover estimates for 2016 are more than €200 billion compared to €185 billion in the previous year. Without recourse factoring is by far the most common form of factoring used by the market (about 70% of total turnover).

Unlike the trend in bank loans, which were severely impacted by the economic crisis that characterised the last 9 years, factoring saw continuous turnover growth of more than 60% over the same period (in 2007, turnover was €120 billion), demonstrating a certain resilience to negative economic events, as well as being clearly anti-cyclical.

The capacity of the sector to support businesses during the downward phase of the cycle is related to the operators' unique approach to managing risks in which evaluation is not limited to the party being financed, but the quality of the factored receivables and the solvency of the debtors are also considered. The attention paid to managing the factored receivables allows for risk to be better contained with respect to normal bank loans.

This further bears out the validity of debtor financing, and factoring in general, from various points of view.

Factoring, as an opportunity for diversification of access to sources of financing for the business world - as in the specific case small and medium enterprises - which is often subject to considerable credit restrictions imposed by the traditional banking industry, has contributed productively to providing financial support for business continuity and growth.

Credit management services, with the constantly expanding skillset possessed by factoring companies, permit considerable simplification of relationships between the participants in the system, which, in the absence of structural changes in Italy, promote a

virtuous process aimed at ensuring better performance in the monetisation of the expected cash flows of suppliers. In addition, for large companies, factoring services, especially factoring without recourse, are of strategic importance due to their significant contribution to improving net financial position. This first clear advantage is accompanied by the possibility, through servicing, of receiving full support in solving critical issues in relations with debtors - consider, for example, the public administration - thanks to the specialisation and far-reaching local monitoring ability assured by the most well organised operators.

The analysis of the data provided by ASSIFACT further emphasises that, from the operators' perspective, the Italian market still appears quite concentrated: with over 60% of turnover in 2016, market share is solidly in the hands of the top three factoring companies.

In the Italian market, one of the most important in the world, the demand for factoring services towards the Public Administration represents a significant portion of the market. According to Assifact estimates, around 30% of outstanding receivables are Public Administration debtors, while the sector's exposure is 25%.

Despite the efforts made by the Government with the enactment of Legislative Decree no. 35 of 8 April 2013, converted by Law no. 64 of 6 June 2013 with the aim of rectifying the payment of certain, liquid and collectable pre-existing Public Administration debt through the allocation of about €40 billion and the transposition of the EU regulation on late payments that exacerbated the amount of late payment interest for payments beyond 60 days, public entities continue to have difficulties in fulfilling payment commitments at agreed due dates.

In this regard, mention is quite frequently made in the Italian press of the constant difficulties in relations between suppliers and government entities, as a result of which Italy is still today the worst payer in Europe, with average payment times that are still above 130 days compared the European average of 45 days.

In the interest of completeness, it should be noted that, while there are still considerable difficulties in properly identifying actual values, recent sources in the press indicate that the stock of outstanding, unpaid receivables is estimated at approximately €65 billion.

If a particular segment of the public administration is considered, namely goods and services provided to Italy's National Health Service, the average payment times reach and exceed 140 days (according to Assobiomedica).

From a geographical standpoint, regional payment performance is rather well defined and may be broken down into three different groups:

Up to 90 days past due: Valle d'Aosta, Friuli Venezia Giulia, Trentino Alto Adige, Lombardy, Marche, Liguria and Veneto.

Up to 180 days past due: Emilia Romagna, Umbria, Basilicata, Abruzzo, Puglia, Tuscany, Lazio and Piedmont.

More than 180 days past due: Sardinia, Sicily, Campania, Calabria, and Molise.

In addition, in 2016 the regions with the greatest density of companies remained those in which factoring was most common (Lombardy, Lazio and Piedmont).

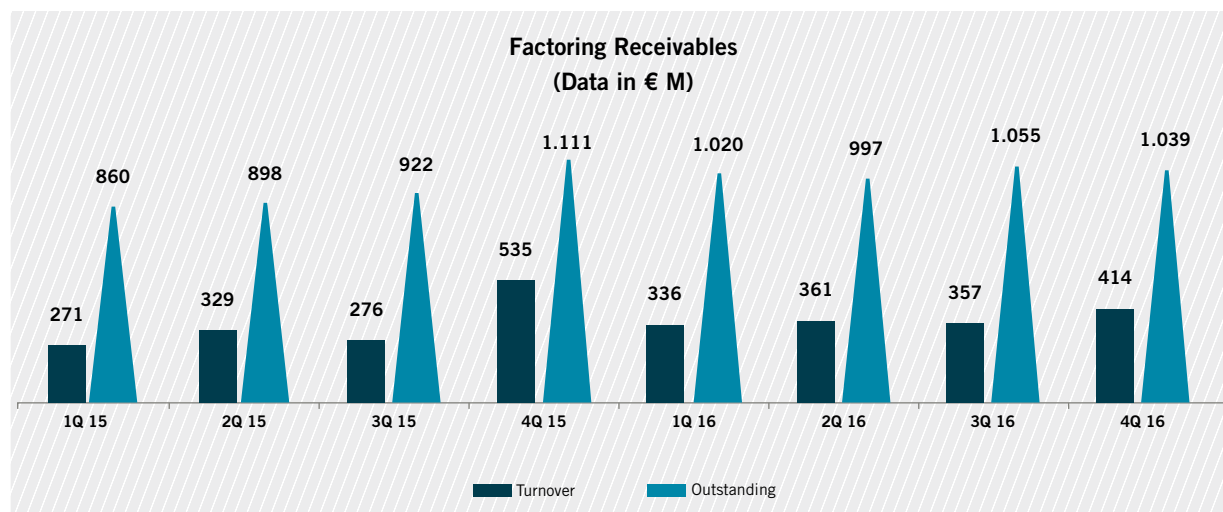
Considering these statistics, for suppliers the assignment of receivables from public entities, especially without recourse, continues to represent an important tool for rebalancing their finances and entrusting credit collection to third parties. In this context, the sector performs, and will continue to perform, an important role in supporting SMEs even in relation to the difficulties in lending that have come forth in banking system because of increased risk and the subsequent capital reinforcement requirements from the Supervisory Authorities.

The significant growth of factoring in recent decades bears witness to the strategic value of this service in supporting the economic system. In the light of recent developments in the European political situation, the sector's prospects remain stably tied to aspects of development (factoring of tax credits, export factoring, etc.) capable of guaranteeing further margins of volume growth and extension to new services.

The Banca Sistema Group and factoring activities

The turnover for the period ended December 2016 for the Banca Sistema Group was €1,469 million (of which €15 million attributable to Beta), up 4% on the same period in 2015.

Considering the third-party receivables managed, total volumes amount to €1,761 million as at 31 December 2016.

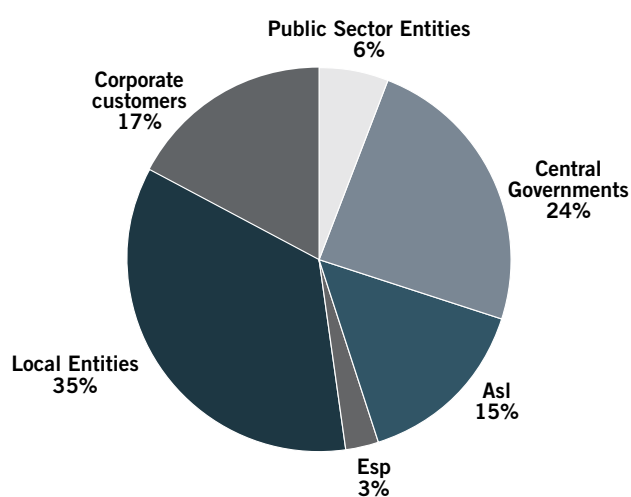


Outstanding loans as at 31 December 2016 amounted to €1,039 million, impacted by the trend in turnover in 2016 and by collections in the period, down 7% on the €1,111 million recorded at 31 December 2015, mainly due to the collection trend in 2016, which was higher than receivable portfolios acquired during the same period.

Collections as at 31 December 2016 stood at €1,550 million, of which €26 million attributable to customers of Beta, up 30% on collections as at 31 December 2015.

The chart below shows the ratio of debtors to the outstanding portfolio as at 31 December 2016.

The Group's core business remains the Public Administration entities segment.



The Group works through both direct assignments by companies and within the framework of regional agreements for restructuring or re-organising public entity debts. These transactions include traditional factoring agreements, as well as reverse factoring agreements with highly reliable public entities, which are seeking to use factoring with their suppliers in their role as debtors.

The following table shows the factoring turnover by product type:

TURNOVER (€ M)	31/12/2016	31/12/2015	€ Change	% Change
Trade receivables	1,305	1,270	35	3%
<i>of which, without recourse</i>	<i>1,008</i>	<i>1,096</i>	<i>(88)</i>	<i>-8%</i>
<i>of which, with recourse</i>	<i>297</i>	<i>174</i>	<i>123</i>	<i>71%</i>
Tax receivables	163	142	22	15%
<i>of which, without recourse</i>	<i>142</i>	<i>123</i>	<i>19</i>	<i>15%</i>
<i>of which, with recourse</i>	<i>21</i>	<i>18</i>	<i>3</i>	<i>14%</i>
TOTAL	1,469	1,411	57	4%

Tax receivables as at 31 December 2016 increased (+15%), partly due to the introduction of split payments in 2015, and include VAT credits from insolvency proceedings as well as IRES receivables. The number of customers in December 2016 increased to 363 (of

which 26 belong to Beta), up 23% (up 15% if Beta is not considered) compared to 2015 due to the strengthening of indirect factoring for the PA and private debtors, the extension of the sales network which began in 2015, and as a result of the agreements entered into with banks.

Collection and debt recovery activities

For the purposes of its debt recovery activities, the Group uses both its own internal structures, and a network of external operators and companies specialised in debt recovery that are active across the entire country. The network of freelancers used by the Bank enables an exact adjustment of the debt collection activities with regard to each specific debtor or an increase in the number of operators when it becomes necessary to focus on specific areas.

In December 2016, collections managed by the Bank under its credit factoring portfolios totalled €1,550 million (up 30% on 2015).

Recovery and reconciliation of collections is divided into out-of-court recovery activity, when invoices are paid according to the internally estimated schedule, and legal recovery activity. In particular, the policy for managing and recovering receivables claimed by Banca Sistema from the public administration has been

characterised, since the launch of the business, by an approach that involves legal action only after an out-of-court recovery process.

Clearly, legal action remains the sole remedy available in the event of voluntary non-payment or failure to reach out-of-court agreements with the factored debtor. In particular, legal action is initiated when it is necessary to avoid a loss for the Bank. In addition, the recovery of the late payment interest component is necessary in some cases in order to achieve the expected profitability. It should be noted that, due to an inefficient judicial system, as often remarked in many institutional settings, the transition from out-of-court collection to legal collection has the consequence of extending collection times for this latter component. Accordingly, even if the receivables amount subject to legal action remains on average below 10% of the total receivables acquired each year, the effect of delay in the Italian

judicial system results in the stratification of the timetable for such receivables subject to legal action and means that 23% of outstanding receivables at the end of December 2016 consisted of receivables subject to legal action.

At the close of the first half of 2016, the Bank revised its accounting treatment of late payment interest on the loans in the legal action portfolio, transitioning from cash accounting to accrual accounting on 30 June 2016.

During the fourth quarter of 2016, in light of the

expansion and improvement of the data base related to historically observed collection of late payment interest and the inclusion of the historical collection data series from Beta Stepstone (acquired on 1 July 2016), the Bank implemented a statistical model to determine the expected percentage of recovery.

The adoption of this model has led to an increase, in the income statement, in the expected recovery percentage of late payment interest for debtors of the national health system, which went from 15% to 65%.

Servicing activities

Through its network of collectors, the Group manages and reconciles the collection of invoices of third customers.

As at 31 December 2016, the amount of third-party receivables managed by the Group totalled €292 million, while the fee and commission income generated by this business segment totalled €968 thousand.

BANKING

Direct funding

The funding policy of the banking division is strictly linked to changes in trade loans and market conditions.

Retail funding accounts for 51% of the total and is composed of the account Si Conto! Corrente and the product SI Conto! Deposito.

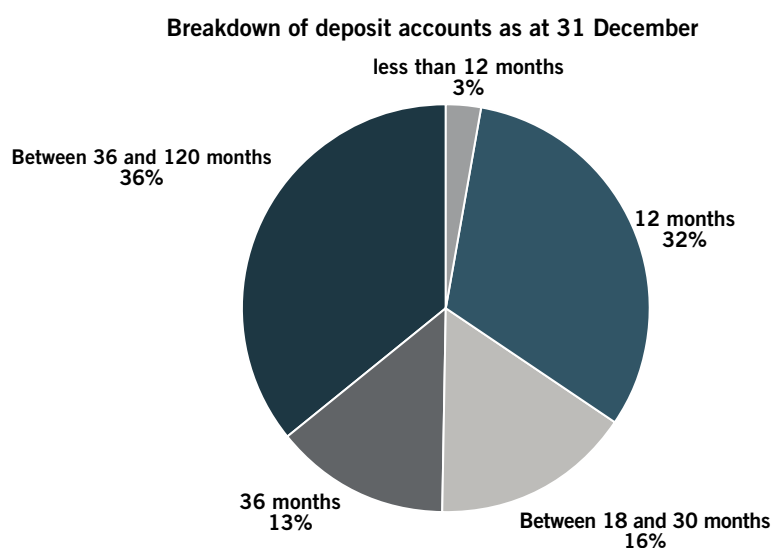
Total term deposits as at 31 December 2016 amounted to €443 million, a decrease of €114 million compared to 31 December 2015. The decrease was due to a specific decision by the Bank that is in line with the strategy to diversify funding sources and with a view of optimising

costs. Requests for early redemption or withdrawals from accounts were modest (-10%), in keeping with normal performance.

The above-mentioned amount also includes total term deposits of €117 million (obtained with the help of a partner platform) held with entities resident in Germany and Austria (accounting for 26% of total deposit funding), an increase of 78 million over the previous year. The increase benefited from the increase in interest rates in Germany over the course of the year.

There were 11,162 individual customers with term deposits as at 31 December 2016, an increase compared with the figures as at 31 December 2015 (10,693). The average deposit was €39 thousand, down compared with the figures as at 31 December 2015 (€52 thousand).

The breakdown of funding by term is shown below.



Current accounts increased from 3,632 (as at 31 December 2015) to 4,111 in December 2016, while the current account balance as at 31 December 2016 was €451 million, up €116 million compared with 31 December 2015.

Indirect funding

Indirect funding from assets under administration as at 31 December 2016 amounted to €113 million (€ 364 million as at 31 December 2015). The breakdown is as follows:

Type (€ M)	31/12/2016	31/12/2015	€ Change	% Change
Bonds	25,162	123,037	(97,875)	-79.5%
Equities	77,945	232,575	(154,630)	-66.5%
Warrants	44	319	(275)	-86.2%
Funds	10,327	8,177	2,150	26.3%
TOTAL	113,478	364,108	(250,630)	-68.8%

Guaranteed loans to small and medium-sized enterprises

Granting loans to SMEs guaranteed by the Guarantee fund of the Ministry of Economic Development (Law 662/96) is an instrument that enables companies to access secured credit, and the Group to grant loans with low risk of impact on the capital in view of the State guarantee (up to 80%); the average guarantee coverage for the Group is 80%.

In light of the new regulatory measures that are about to be introduced on guarantees to this type of loan, the

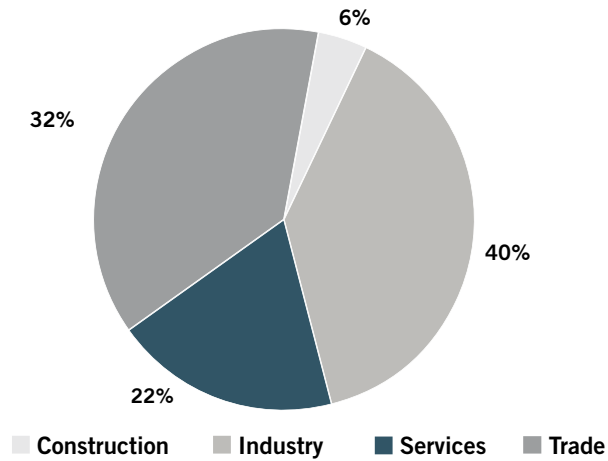
Bank has decided to suspend granting guaranteed loans to SMEs, redirecting the resources dedicated to SME loans to a segment where there is deemed to be more room for growth, such as salary- and pension-backed loans, also thanks to strategic agreements currently being discussed with leading originators.

As at 31 December 2016, the Group disbursed €30.0 million (€79.0 million in December 2015), with €79 million outstanding at the end of the period.

	31/12/2016	31/12/2015	€ Change	% Change
No. of applications	90	188	(98)	-52%
Volumes disbursed	30,030	79,015	(48,985)	-62%

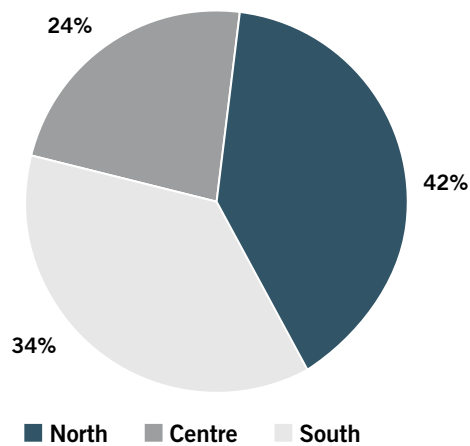
As shown in the graphs below, the geographical areas and sectors are quite varied, thus enabling the Group to benefit from a highly diversified portfolio.

Outstanding PMI - Breakdown by sector



The breakdown of volumes disbursed by geographical area is shown below.

Area Volumes disbursed to SME - Breakdown by geographical area



Salary-backed loans (CQS) and Pension-backed loans (CQP)

The Banca Sistema Group entered the salary- and pension-backed loan (CQS/CQP and to a lesser extent, salary deductions) market in 2014, through the acquisition from other specialist intermediaries of receivables portfolios derived from this specific type of financing. As at 31 December 2016, the Bank has five ongoing agreements with specialist distributors in the sector. A salary-backed loan (CQS) is a consumer loan product

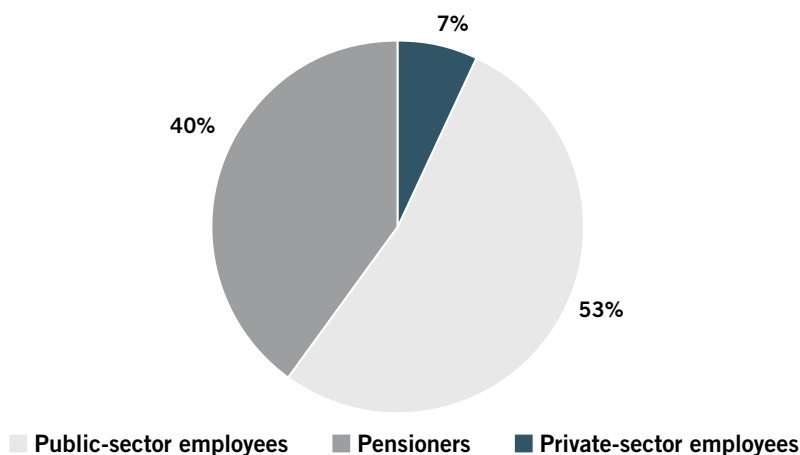
that allows customers to allocate up to a fifth of their salaries to the payment of loan instalments.

The volumes acquired from the beginning of the year until December 2016 amounted to €156.7 million, including private-sector employees (7%), pensioners (40%) and public-sector employees (53%). Therefore, over 93% of the volumes refer to pensioners and employees of the PA, which remains the Bank's main debtor.

	31/12/2016	31/12/2015	€ Change	% Change
No. of applications	7,641	5,526	2,115	38%
Volumes disbursed	156,691	114,894	41,797	36%

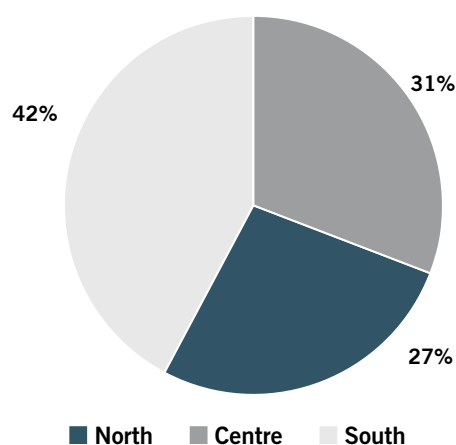
As shown in the table, the amounts disbursed in 2016 were considerably higher than in 2015 as a result of the agreements concluded by the Bank during 2015.

CQS disbursed volumes - Breakdown



The geographical breakdown of the pension- and salary-backed loan portfolio is shown below:

CQS disbursed volumes - Breakdown by geographical area



TREASURY ACTIVITIES

Treasury portfolio

A treasury portfolio has been established in order to support liquidity commitments through short-term investment in Italian government bonds.

In 2016, the consistency and the duration of the securities portfolio were down considerably compared to the end of 2015 given that the historically low yields on government bonds were not in line with the volatility expectations that impacted the market for a large part of 2016 (Brexit - the constitutional referendum and government crisis - review of Italy's credit rating).

The nominal value of the treasury portfolio amounts to €507 million compared to €920 million as at 31 December 2015, with a duration of 6.7 months (9.1 months at 31 December 2015).

In 2016, transactions involving government bonds totalled €3.4 billion (against €9.8 billion traded in 2015).

Government bonds are mainly traded on the MTS Italian markets (in which the Bank trades as a market dealer), the European Bond Market (EBM) and through the deal-to-client platforms BondVision and BrokerTec.

Wholesale funding

As at 31 December 2016, wholesale funding was about 49% of the total, comprising a new bond issue, repurchase agreements traded on the MTS MMF Repo platform, inter-bank deposits and refinancing operations with the ECB (58% as at 31 December 2015).

In 2016, trading on the MMF Repo screen-based market totalled about €82 billion compared to €115 billion in 2015.

Participation in the TLTRO II operation proposed by the European Central Bank was settled in the amount of €122.85 million on 29 June, with maturity on 24 June 2020.

The issue of the €70 million senior bond maturing on 03 May 2018, placed with institutional investors, allowed diversification of the sources of funding and a significant increase in duration of the sources of funding, whereas the securitisation of salary-backed loans allowed positions to be refinanced more efficiently than the traditional types of funding.

The Group also used the interbank deposit market both through the e-MID market and through bilateral agreements with other banks. In particular, it should be noted that the securitisation of Quinto Sistema Sec.

2016, completed with a partly-paid securities structure and "progressive growth of the securitised portfolio" (a "warehouse" structure) permitted an efficient and effective source of funding dedicated to the CQS portfolio to be maintained throughout the year. In fact, during 2016, through the conclusion of successive guaranteed refinancing agreements (over the counter REPOs), the securitised senior notes were refinanced with more advantageous conditions with respect to the traditional types of funding up until the time they were officially eligible as collateral for Eurosystem refinancing transactions, as they are at 31 December 2016.

Existing bank deposits amounted to €300 million, compared to €282 million as at 31 December 2015. In 2016 trading volumes were €2.2 billion, compared to €2.8 billion in 2015.

The listing of the shares of Banca Sistema on the Milan Stock Exchange permitted a sharp improvement in interbank relations, facilitating the granting of MM lines of credit. Such funding allows short-term treasury needs to be met by exploiting the extremely low level of interest rates, with the possibility of drawing funds from the interbank market in a manner useful to diversifying funding.

THE MAIN BALANCE SHEET AGGREGATES

The comments on the main aggregates on the asset side of the statement of financial position are shown below.

ASSETS (€,000)	31/12/2016	31/12/2015	€ Change	% Change
Cash and cash equivalents	98	104	(6)	-5.8%
Financial assets held for trading	996	-	996	n.a.
Financial assets available for sale	514,838	925,402	(410,564)	-44.4%
Due from banks	83,493	2,076	81,417	3921.8%
Loans to customers	1,348,329	1,457,990	(109,661)	-7.5%
Equity investments	1,030	2,696	(1,666)	-61.8%
Property and equipment	23,313	1,058	22,255	2103.5%
Intangible assets	1,835	1,872	(37)	-2.0%
<i>of which: goodwill</i>	<i>1,786</i>	<i>1,786</i>	<i>-</i>	<i>0.0%</i>
Tax assets	10,528	7,353	3,175	43.2%
Other assets	14,903	13,119	1,784	13.6%
Total assets	1,999,363	2,411,670	(412,307)	-17.1%

The 2016 financial year ended with total assets of €2 billion, down 17% on 2015, mainly as a result of the decision to maintain a reduced exposure to Italian government bonds (-45%) and the changes in collections of factored receivables, which affected the stock at the end of the period.

The scope of the Group's consolidated financial statements changed due to the incorporation of the vehicle Largo Augusto Servizi e Sviluppo S.r.l. (LASS), with fully paid-in capital of €4 million. On 31 August 2016, the subsidiary, using a loan from the Parent Company, purchased a property for €21.5 million that

will be used as the Bank's new headquarters once the planned renovation work has been completed.

In addition, on 1 July 2016 the acquisition of Beta Stepstone S.p.A. (hereinafter "Beta") was finalised for final consideration of €56.7 million, net of various contractual reductions and adjustments of €3.5 million. During the acquisition process, the amount of late payment interest receivable not yet collected by Beta was placed in an escrow account, release of which to the seller is conditional solely on the collection of that late payment interest, fully securing the receivable in question.

The following is a provisional allocation of the purchase price, based on Beta's acquisition shareholders' equity at 30 June 2016, in accordance with IFRS 3.

PROVISIONAL ALLOCATION OF THE PURCHASE PRICE (€,'000)

Purchase price	56,707
Elimination of Beta's shareholders' equity	(60,168)
Residual value to be allocated	(3,461)
Allocation to the provision for risks and charges	3,326
Credit risk adjustments	1,608
Recognition of deferred tax assets	(1,524)
Other costs borne by the seller	51
Total provisional allocation	3,461

The amount allocated to the provision for risks represents an estimate of possible future charges due to litigation and disputes, determined during the acquisition process, whereas credit risk adjustments have been provisionally recognised based on the measurement of Beta's loan portfolio at fair value. The allocation to those captions was made gross of tax effects, with the related recognition of deferred tax assets.

The Bank's AFS (available-for-sale) securities portfolio is mainly comprised of Italian government bonds with an average remaining duration of about 7 months as at 31 December 2016 (the average duration at the end of 2015 was 9 months) and is in line with the Group investment policy to retain securities with durations under 12 months. The government bond portfolio amounted to €508 million

(€920 as at 31 December 2015). The valuation reserve for government securities was €221 thousand net of tax. The AFS portfolio also includes 200 stakes of the Bank of Italy with a value of €5 million purchased in July 2015 and the value at 31 December of the Axactor security, which represented the part of the price paid in the form of shares within the framework of the agreement for the sale of the shares of CS Union. Since 31 December, that security's fair value increased by €458 thousand, net of the tax effect of €226 thousand, thus resulting in a period-end value of €2.0 million.

The increase in the item 'due from banks' can be attributed to liquidity funding in the ECB account and €12 million deposited in an escrow account securing late payment interest as described above.

LOANS TO CUSTOMERS (€,'000)

	31/12/2016	31/12/2015	€ Change	% Change
Factoring	986,169	1,049,832	(63,663)	-6.1%
Salary-/pension-backed loans (CQS/CQP)	265,935	120,356	145,579	121.0%
Loans to SME	78,975	83,110	(4,135)	-5.0%
Reverse repurchase agreements	-	177,868	(177,868)	-100.0%
Current accounts	12,255	13,906	(1,651)	-11.9%
Compensation and Guarantee Fund	4,684	12,486	(7,802)	-62.5%
Other receivables	311	432	(121)	-28.0%
Total	1,348,329	1,457,990	(109,661)	-7.5%

"Loans to customers" mainly comprise outstanding loans for factoring receivables, down from 82% to 73% in the item. Salary- and pension-backed loans grew by more than 100% compared to the end of 2015 as a result of newly acquired volumes equal to €157 million, while government-backed loans to SMEs remained generally in line with 2015, as disbursements partially offset collections during the period.

As at 31 December 2016 the book value of factoring receivables is down by 6.1% on 31 December 2015, mainly as a result of the trend in collections recorded in 2016 (€1,550 million). The figure includes €69 million outstanding attributable to Beta. The cumulative turnover figure at 31 December 2016 thus amounted to €1,453 million (€1,411 million in the previous year). The number of turnover-generating customers during 2016 was 337, of which 192 were new customers in 2016.

As mentioned above, securitisation of salary-backed

loans began in 2016, as projected in the business plan. The amount of the receivables factored to the special-purpose vehicle in four different periods was €197.9 million (€182.3 million outstanding at the end of the period), compared to the ABSs of the special-purpose vehicle Quinto Sistema S.r.l. (the SPV), fully subscribed by the Bank, of a total €190 million at 31 December 2016.

On 19 October, Moody's and DBRS assigned ratings to the Class A (Senior) and Class B (Mezzanine) notes. On 20 October, the notes were listed on the Luxembourg Stock Exchange and the prospectus, which complies with the Prospectus Directive, was published.

Since the securities are completely held by the Bank, the conditions for derecognition of the loans have not been met. Therefore, the loans have been re-recorded in the accounts as assets sold and not derecognised with a balancing entry against the subscribed asset-backed securities (ABS).

The following table shows the quality of receivables in the 'loans to customers' item, without considering the amount relating to reverse REPOs during the periods in which that investment was present.

STATUS	31/12/2015	31/03/2016	30/06/2016	30/09/2016	31/12/2016
Bad loans	20,021	23,426	29,936	36,019	35,231
Unlikely to pay	5,913	4,722	10,586	11,133	20,189
Overdue payments/defaults>180 days	65,420	64,395	64,664	96,028	68,342
Non-performing	91,354	92,543	105,186	143,180	123,762
Performing	1,172,410	1,111,123	1,085,778	1,150,176	1,242,832
Other loans to customers (excluding REPOs)	26,729	28,995	15,293	19,670	4,033
Total excluding REPOs	1,290,493	1,232,661	1,206,257	1,313,026	1,370,628
Individual adjustments	7,137	8,284	9,969	12,109	16,457
Collective adjustments	3,233	3,557	3,531	4,198	5,842
Total adjustments	10,370	11,841	13,500	16,307	22,299
Net exposure	1,280,123	1,220,820	1,192,757	1,296,719	1,348,329

The ratio of net non-performing loans to the total in the portfolio (net of reverse repos) is up from 7.1% as at 31 December 2015 to 9.0% as at 31 December 2016, mainly due to increases in bad loans and unlikely to pay. Net bad loans amounted to 1.7% of total loans to customers, remaining at moderate levels. The increase in the quarter in loans classified as “unlikely to pay” is mainly due to a deterioration in factored receivables due from public companies, and to a lesser extent, from loans to SMEs. The amount of past due loans is mainly attributed to factoring receivables without recourse from the Public Administration and is considered normal for the sector and does not represent an issue in terms of credit quality and probability of collection.

During the quarter, the provision for value adjustments increased as a result of an increase of up to 100% in the value adjustment percentage on the SME portfolio from a thorough and more prudent overall assessment of 20% of the portfolio that is not guaranteed by the Guarantee fund of the Ministry of Economic Development, and from the value adjustments on specific factoring positions between private parties.

The coverage ratio of bad loans has increased to 34.8% as at 31 December 2016 (30.6% as at 31 December 2015): this percentage, since it is impacted by factoring of receivables from distressed local authorities, is entirely appropriate.

The Bank is completing a process related to a valuation model for the provision for bad loans deriving from Public Administration debtors on Factoring products,

the first results of which give a higher probability of recovery than what is currently estimated.

Compared to the end of the previous year, there were no temporary investments in reverse repurchase agreements (€178 million at the end of 2015). The amounts of the cash used in the Compensation and Guarantee Fund to finance transactions in repurchase agreements with bank customers decreased significantly due to the reduction of the securities portfolio.

Equity investments include the Bank's current equity stake of 10.0% in CS Union S.p.A., a company operating on the financial and commercial bad loans management market, as well as in the management and recovery of receivables between individuals. As previously described, in the context of the strategic collaboration agreement between Banca Sistema and Axactor, in the second quarter of 2016 the Bank finalised the sale to Axactor of the 15.8% equity interest held in CS Union, recording a capital gain of €2.3 million. The price of sale was settled 60% in cash and the remainder in shares of Axactor.

Property and equipment includes the property located in Milan, which will primarily be used as Banca Sistema's new offices following the completion of the renovation work, scheduled for the fourth quarter of 2017. The book value of the property, inclusive of taxes paid, is €22.4 million.

Other assets include amounts being processed after the end of the reference period and advance tax payments of approximately €10 million.

Comments on the main aggregates on the liability side of the statement of financial position are shown below.

LIABILITIES AND SHAREHOLDERS' EQUITY (€,'000)	31/12/2016	31/12/2015	€ Change	% Change
Due to banks	458,126	362,075	96,051	26.5%
Due to customers	1,262,123	1,878,339	(616,216)	-32.8%
Securities issued	90,330	20,102	70,228	349.4%
Tax liabilities	8,539	804	7,735	962.1%
Other liabilities	59,825	55,317	4,508	8.1%
Employee termination indemnities	1,998	1,303	695	53.3%
Provisions for risks and charges	4,105	372	3,733	1003.5%
Valuation reserves	425	350	75	21.4%
Reserves	78,980	65,750	13,230	20.1%
Share capital	9,651	9,651	-	0.0%
Treasury shares (-)	(52)	-	(52)	n.a.
Profit for the period/year	25,313	17,607	7,706	43.8%
Total liabilities and shareholders' equity	1,999,363	2,411,670	(412,307)	-17.1%

Wholesale funding represents about 49% of the total (58% as at 31 December 2015), down compared to the end of 2015 due to a decrease in repurchase agreements traded through the MTS platform (classified under 'due to customers', since there is no direct balancing entry with banks).

There was an increase in the weight of bond funding, which rose from 2% to 11% of the total wholesale funding, thanks to the private placement of a senior bond of €70 million maturing in two years, as well as the greater use of funding from the ECB.

DUE TO BANKS (€,'000)	31/12/2016	31/12/2015	€ Change	% Change
Due to Central banks	192,850	80,002	112,848	141.1%
Due to banks	265,276	282,073	(16,797)	-6.0%
<i>Current accounts and demand deposits</i>	<i>20,276</i>	<i>10,328</i>	<i>9,948</i>	<i>96.3%</i>
<i>Term deposits</i>	<i>245,000</i>	<i>271,745</i>	<i>(26,745)</i>	<i>-9.8%</i>
Total	458,126	362,075	96,051	26.5%

Amounts due to banks increased compared to 31 December 2016 due to the increase in refinancing operations with the ECB with the ABS from the securitisation of salary- and pension-backed receivables (CQS/CQP) as collateral, which allowed for funding of €120.4 million to be obtained. Retail loans were placed as collateral for the remaining amount. The Bank also participated in the TLTRO II auction for

€123 million, with a duration of four years and current expected rate of -40bps.

This potential revenue was not recognised in that it will only become certain on the maturity date; a rate of 0% was instead considered.

As at 31 December 2016, there was a funding on the interbank market in the form of term deposits with an average duration of about 2 months.

DUE TO CUSTOMERS (€,'000)	31/12/2016	31/12/2015	€ Change	% Change
Term deposits	443,396	572,379	(128,984)	-22.5%
Funding (repurchase agreements)	295,581	909,089	(613,509)	-67.5%
Current accounts and demand deposits	436,986	335,574	101,412	30.2%
Deposits with Cassa Depositi e Prestiti	35,615	30,603	5,012	16.4%
Due to assignors	50,547	30,694	19,853	64.7%
Total	1,262,123	1,878,339	(616,216)	-32.8%

The period-end stock of term deposits was down 22.5% on the end of 2015, reflecting net negative deposits (net of interest accrued) of €126.5 million; gross deposits from the beginning of the year were €425.4 million, against withdrawals caused mainly by non-renewals totalling €551.9 million.

The reduction in funding from deposit accounts is in line with the Bank's need to diversify and contain the costs of funding.

Funding from repurchase agreements was also down mainly as a result of the smaller securities portfolio. Amounts due to customers also include funding of €34.8 million from Cassa Depositi e Prestiti obtained against collateral consisting solely of loans to SMEs by the Bank.

Other amounts due include payables related to receivables acquired but not funded. The balance of debt securities issued increased compared to 31 December 2016 due to the new issue of bonds placed with institutional customers. The item's composition was as follows:

- Tier 2 subordinated loan of €12 million, set to mature on 15 November 2022;
- Tier 1 subordinated loan of €8 million, with no maturity (perpetual basis);
- senior bond of €70 million, set to mature on 3 May 2018.

The provision for risks and charges of €4.1 million includes the amount of €3.3 million, representing the

estimated future liabilities attributable to Beta, calculated based on the provisional price allocation in accordance with IFRS 3.

The remainder refers to the portion of the 2015 bonus deferred to the following three years.

Some service providers have recently initiated legal action seeking payment of consideration for services rendered that, in the Bank's opinion, did not require any additional provisions.

It should be noted that in December, the Italian Revenue Office issued two assessment notices to the Beta subsidiary regarding the 2011 tax year (one assessment regarding transfer pricing for €1.093 thousand, and the other for withholding tax for €1.404 thousand).

A specific provision for these assessments was not made since the Company feels that it has fully complied with the regulations and intends to present its case in the appropriate forum. In this regard, on 10 February 2017 the Company filed a tax settlement proposal with the Revenue Office to establish a cross examination and to restate that the claims made were devoid of any merit, since the company acted appropriately in consistently applying the transfer pricing and in total respect of the regulatory requirements including with regard to the withholding tax.

'Other liabilities' mainly include payments received after the end of the period from the assigned debtors and which were still being allocated and items being processed during the days following period-end, as well as trade payables and tax liabilities.

The reconciliation between the net result and shareholders' equity of the parent company and the figures from the consolidated financial statements is shown below.

(€ ,000)	NET RESULT	SHAREHOLDERS' EQUITY
Net result/Parent Company Shareholders' equity	24,481	113,635
Assumption of value of investments	-	(60,598)
Net result/shareholders' equity - subsidiaries	832	61,279
Consolidated shareholders' equity	25,313	114,316
Minority shareholders' equity	-	20
Group Shareholders' equity	25,313	114,296

CAPITAL ADEQUACY

Due to the acquisition of Beta and the incorporation of LASS, it is no longer possible to opt out of consolidated financial reporting. Accordingly, financial reporting was produced on a consolidated basis starting from the third

quarter of 2016.

Provisional information concerning the regulatory capital and capital adequacy of the Banca Sistema Group is shown below.

OWN FUNDS (€ ,000) AND CAPITAL RATIOS	31/12/2016	31/12/2015 (*)
Common Equity Tier 1 (CET1)	104,621	86,892
TIER1	8,000	8,000
Additional Tier 1 capital (AT1)	112,621	94,892
TIER2	12,092	12,000
Total Own Funds (TC)	124,713	106,892
Total risk weighted assets	788,041	635,658
of which, credit risk	652,999	535,194
of which, operational risk	130,447	100,464
of which, market risk	4,595	0
Ratio - CET1	13.3%	13.7%
Ratio - T1	14.3%	14.9%
Ratio - TCR	15.8%	16.8%

(*) Figures based on separate reporting by Banca Sistema

Total own funds were €125 million as at 31 December 2016 and included the profit for 2016, net of dividends estimated on the profit for the year of 2016 of €6.1 million. The estimate was made based on a pay-out of 25% of the Parent Company's profit.

The increase in RWAs compared to 31 December 2015, in addition to the impact of Beta Stepstone,

consolidated at 30 September 2016 (approximately €27 million in terms of RWAs) but absent from the scope of consolidation at 31 December 2015, was primarily due to the increase in loans, particularly salary- and pension-backed loans, the increase in past-due loans to the public administration and the purchase of the property.

CAPITAL AND SHARES

Capital and ownership structure

The share capital of Banca Sistema is composed by 80,421,052 ordinary shares, for total paid-in share capital of € 9,650,526.24. All outstanding shares have regular dividend entitlement from 1 January.

Based on evidence from the Shareholders' Register and

more recent information available, as at 18 January 2017 the shareholders with stakes of more than 5%, the threshold above which Italian law (art. 120 of the Consolidated Law on Finance) requires disclosure to the investee company and Consob, were as follows:

SHAREHOLDERS	% HELD
SGBS S.r.l. (Management Company)	23.1%
Garbifin	0.5%
Fondazione Sicilia	7.4%
Fondazione Cassa di Risparmio di Alessandria	7.4%
Fondazione Pisa	7.4%
Schroders	6.7%
Market	47.5%

Treasury shares

As at 31 December 2016, Banca Sistema held 25,000 treasury shares ("Treasury Shares") to service the incentive plans for the Group's key personnel, i.e. an equity interest of 0.031%.

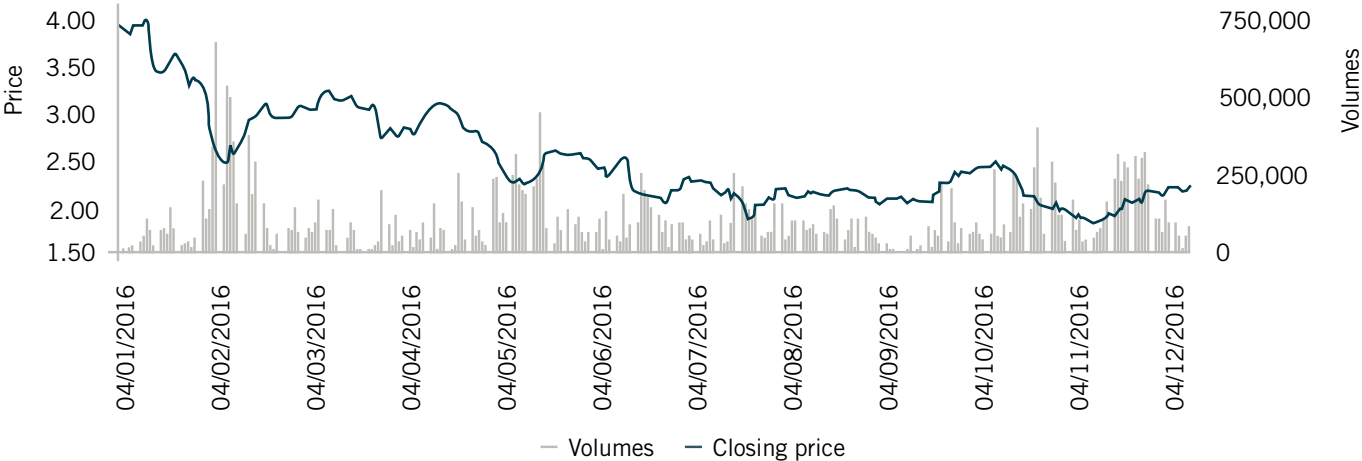
Stock performance

The shares of Banca Sistema are traded on the Mercato Telematico Azionario - Italian Equities Market (MTA) of the Italian Stock Exchange, STAR segment. The Banca Sistema stock is included in the following Italian Stock Exchange indices:

- FTSE Italia All-Share Capped;
- FTSE Italia All-Share;
- FTSE Italia STAR;
- FTSE Italia Servizi Finanziari;
- FTSE Italia Finanza;
- FTSE Italia Small Cap.

The following table presents stock performance from 4 January 2016 to 30 December 2016.

Price trend



Source: Bloomberg

ECONOMIC RESULTS

INCOME STATEMENT (€,'000)	31/12/2016	31/12/2015	€ Change	% Change
Interest margin	71,000	58,006	12,994	22.4%
Net fee and commission income	9,060	11,168	(2,108)	-18.9%
Dividends and similar income	227	-	227	n.a.
Profit (Loss) on trading	(84)	122	(206)	-168.9%
Profit from disposal or repurchase of financial assets	1,280	2,518	(1,238)	-49.2%
Net interest and other banking income	81,483	71,814	9,669	13.5%
Net value adjustments due to loan impairment	(9,765)	(5,439)	(4,326)	79.5%
Net income from banking activities	71,718	66,375	5,343	8.0%
Personnel expenses	(15,169)	(13,139)	(2,030)	15.5%
Other administrative expenses	(20,907)	(20,112)	(795)	4.0%
Net allowance for risks and charges	(431)	300	(731)	-243.7%
Net value adjustments to property and equipment/intangible assets	(308)	(312)	4	-1.3%
Other operating income (expenses)	150	71	79	102.7%
Operating expenses	(36,665)	(33,192)	(3,473)	10.5%
Profit (loss) from equity investments	2,281	422	1,859	440.5%
Profit (Loss) from disposal of investments	-	534	(534)	-100.0%
Profit from current operations before taxes	37,334	34,139	3,195	9.3%
Income taxes for the period	(10,926)	(10,426)	(500)	4.8%
Parent company profit for the period	26,408	23,713	2,695	11.4%

The 2016 annual results, with respect to 2015, include the contribution of the Beta Stepstone subsidiary which generate profits of €1.3 million in the six months following the acquisition.

It should also be noted that the 2016 results were normalised to exclude the extraordinary contribution to the National Resolution Fund of €1.3 million (€0.9 million net of tax) and costs related to the integration of Beta for €0.3 million, both of which are classified under the 'other administrative expenses'. It should also be recalled that the economic results at 31 December 2015 have been normalised in order to eliminate the extraordinary contribution to the National Resolution Fund (FRN) of €1.9 million (€1.3 million net of tax) and non-recurring costs pertaining to the listing process

included in personnel expenses and other administrative expenses of €6.7 million (€4.9 million net of tax).

The 2016 financial year closed with a profit of €26.4 million, an increase of 11.4% over 2015, mainly as a result of increased interest margins that more than offset the increased loan value adjustments and higher operating costs. As described above, the increase in the interest margin was due in part to the recognition of €11.3 million of late payment interest, which represents the portion of the late payment interests accrued at 31 December 2016 that may reasonably be expected to be recovered: before 30 June 2016, late payment interest was recognised on a cash basis.

On 30 June 2016, the Bank revised its accounting treatment of late payment interest in accordance with

IFRS as a result of the experience gained and the systematic implementation of out-of-court and judicial recovery measures for past-due receivables, transitioning from cash accounting to accrual accounting only for receivables subject to legal action. On average, the percentage of total receivables acquired each year that are subject to legal action is less than 10%. During the fourth quarter of 2016, in light of the expansion and improvement of the data base related to historically observed collection, the inclusion of the historical data series of collections from Beta Stepstone, as well as regulatory clarifications (content of the document regarding the “Financial statement treatment of late payment interest pursuant to Legislative Decree 231/2002 on permanently acquired non-performing positions” of 9 November 2016), the Bank completed an analysis of the recovery estimates and implemented a statistical model to determine the expected percentage

of recovery in order to record them in the income statement. This model, considering the size of series from Beta, resulted in an increase in the expected recovery percentages for debtors of the national health system, which went from 15% to 65% with a resulting increase in the percentage used for financial statement purposes compared to the previous quarters. Whereas for late payment interest on other public administration debtors, despite the late payment interest recovery percentages and the model would have resulted in an allocation percentage greater than 15%.

The recovery percentages used in June were prudently confirmed. Had the Group applied the rates provided by the model, interest income would have been higher by €15.8 million.

The result for 2016 also includes the realised capital gain deriving from the sale of a 15% interest in CS Union to Axactor of €2.3 million.

INTEREST MARGIN (€,'000)	31/12/2016	31/12/2015	€ Change	% Change
Interest and similar income				
Receivables portfolios	86,005	77,685	8,320	10.7%
Securities portfolio	(242)	813	(1,055)	-129.8%
Other	558	521	32	6.1%
Total interest income	86,321	79,019	7,302	9.2%
Interest expense and similar expense				
Due to banks	(1,841)	(1,198)	(643)	53.7%
Due to customers	(11,339)	(18,587)	7,248	-39.0%
Securities issued	(2,141)	(1,228)	(913)	74.3%
Total interest expense	(15,321)	(21,013)	5,692	-27.1%
Interest margin	71,000	58,006	12,994	22.4%

The interest margin improved by 22.4% compared to the previous year due to a significant decrease in the cost of funding and a greater contribution deriving from the salary- and pension-backed loan portfolios. Beta also contributed positively, generating an interest margin of €2.6 million in the six months it was included within the scope of the Group.

As previously described, following the refinement of the internal assessment methods and the greater amount of

data available, part of the late payment interest accrued up to 31 December 2016 has been recognised in the income statement, but solely for invoices subject to recovery through legal action; this total interest (which amounts to 7% of total late payment interest accrued as at 31 December 2016 on invoices collected and still outstanding) represents the amount prudentially estimated and deemed recoverable of the total interest accrued on invoices the recovery of which has passed to

legal action.

Considering the gradual rise in the turnover from factoring, there was an increase in the amount of late payment interest accrued on settled and outstanding invoices, which amounted to approximately €104.3 million, net of the amount already allocated, at 31 December 2016 (€70.2 million on collected invoices). In 2016 the late payment interest collected, primarily on portfolios acquired in previous years, amounted to €5.8 million, compared to €2.9 million in all of 2015. Collections include €0.7 thousand of collections by Beta and €2.3 million from the sale of late payment interest receivables to third parties.

The amount resulting from the change of the estimation methods concerning the recoverability of such interest was €11.3 million, of which €5.7 million as the effect of the change of the estimation method compared to the previous year.

The policy adopted by Banca Sistema in managing and recovering receivables claimed from the Public Administration continues to be characterised by an approach that involves legal action only in cases of voluntary non-payment or when there is a failure to reach out-of-court agreements with the assigned debtor. In particular, legal action is always initiated when it is necessary to avoid a loss for the Bank. In addition, the recovery of the late payment interest component is necessary in some cases in order to achieve the expected profitability. Interest income from the receivables portfolio continues to be mainly composed of revenues generated by the factoring receivables portfolio, which accounts for 85% of total interest income (€2.6 million attributable to

Beta). Due to the reduction in average collection times, profitability declined compared to the previous year, net of the late payment interest component. In 2016, the increase in the tax receivables portfolio contributed to the stability of the contribution of the factoring portfolio. The increase in margin was also driven by the marked growth in interest on the salary-backed portfolios, which rose from €2.6 million to €7.4 million, and in part from the increase on the SME portfolios which contributed about €5.4 million to the total.

The negative performance of the securities portfolio, a result of the ECB's interest rate policy, should be linked to the funding cost which was positive. Overall, the carry trade remains positive.

Other interest income mainly includes income generated by revenue from hot money transactions and current accounts.

Funding costs fell compared with the previous year following a general reduction in market rates, which has had a positive impact on wholesale funding, especially from repurchase agreements, but particularly as a result of a focus on the customer deposit diversification and management policy, which allowed for the substitution of term deposit renewals with lower rates compared to those expiring.

The increase in interest due to banks was primarily due to the cost of funding from other banking institutions, the exposure to which, in 2016, was significantly greater than in 2015.

As a result of the current interbank rates and ECB policies, funding through REPOs did not generate any interest expense.

COMMISSION MARGIN (€,000)	31/12/2016	31/12/2015	€ Change	% Change
Fee and commission income				
Collection activities	968	1,108	(140)	-12.6%
Factoring activities	9,139	10,905	(1,766)	-16.2%
Other	788	729	59	8.1%
Total fee and commission income	10,895	12,742	(1,847)	-14.5%
Fee and commission expense				
Placement	(1,509)	(1,031)	(478)	46.4%
Other	(326)	(543)	217	-40.1%
Total fee and commission expense	(1,835)	(1,574)	(261)	16.6%
Commission margin	9,060	11,168	(2,108)	-18.9%

Net fees and commissions, equal to €9 million, were down by 19%, primarily due to lower commissions on factoring business as a result of lesser use of products with commissions. Commissions on collection activity, related to the service of reconciliation of third-party invoices collected from the public administration are down slightly compared to the previous year, while other fee and commission income, which primarily includes commissions on collection and payment services and the keeping and management of current accounts, remained stable compared to the previous year.

The placement fees and commissions paid to third parties increased due to their close correlation with the increase in the factoring volumes disbursed. Such fees and commissions include the costs of origination of factoring receivables of €759 thousand (up 13% on the same period of last year), while the remainder includes returns to third party intermediaries for the placement of the SI Conto! Deposito product, which grew as a result of the higher volumes placed in Germany. Other commission expenses include commissions for trading third-party securities and for interbank collections and payment services.

RESULTS OF THE SECURITIES PORTFOLIO (€,000)	31/12/2016	31/12/2015	€ Change	% Change
Profit (Loss) on trading				
Profit (loss) realised on trading portfolio debt securities	(84)	122	(206)	-168.9%
Total	(84)	122	(206)	-168.9%
Profit (loss) from disposal or repurchase				
Profit (loss) on AFS portfolio debt securities	1,280	2,518	(1,238)	-49.2%
Total	1,280	2,518	(1,238)	-49.2%
Total profit (loss) from the securities portfolio	1,196	2,640	(1,444)	-54.7%

During 2016, profits generated by the proprietary portfolio made a smaller contribution than in same period of last year due to less favourable market performance. Credit risk adjustments made at 31 December 2016, excluding value recoveries related to late payment

collections of the Beta subsidiary, totalled €10.2 million of which €4.3 million in the fourth quarter mainly after increasing the value adjustment percentage to 100% specifically for the SME portfolio which resulted from a thorough and more prudent overall assessment of 20% of

the portfolio that is not guaranteed by the Guarantee fund of the Ministry of Economic Development, and from the value adjustments on specific factoring positions between private parties classified as “unlikely to pay”. Also, the collective value adjustment percentage of the SME portfolio was increased during the first quarter of 2016.

The analytical adjustments made in the previous quarters were mainly due to the classification of new positions of entities in distress and of new SMEs in the "bad loans" category. The loss rate, following what was illustrated above, amounted to 74 bps, which is up on the previous year.

PERSONNEL EXPENSES (€,'000)	31/12/2016	31/12/2015	€ Change	% Change
Wages and salaries	(11,692)	(10,193)	(1,499)	14.7%
Social security contributions and other costs	(2,420)	(2,291)	(129)	5.6%
Directors' and statutory auditors' remuneration	(1,057)	(532)	(525)	98.7%
Total	(15,169)	(13,139)	(2,030)	15.5%

The increase in personnel costs, considering that 2016 includes the personnel costs of Beta amounting to €642 thousand, would have been €1.4 million, or 10%. Headcount increased from 130 to 144 in 2016 (14 of

which belong to Beta).

As at 31 December 2016 the item also includes total costs relating to voluntary redundancy payments of €326 thousand, compared to €206 thousand in the previous year.

OTHER ADMINISTRATIVE EXPENSES (€,'000)	31/12/2016	31/12/2015	€ Change	% Change
Servicing and collection activities	(4,445)	(6,958)	2,513	-36.1%
Resolution Fund	(654)	(617)	(37)	6.0%
Consultancy	(4,756)	(2,817)	(1,939)	68.8%
Computer expenses	(3,735)	(2,990)	(745)	24.9%
Rent and related fees	(1,969)	(1,753)	(216)	12.3%
Indirect taxes and duties	(1,519)	(1,563)	44	-2.8%
Advertising	(204)	(512)	308	-60.2%
Auditing fees	(309)	(262)	(47)	17.9%
Other	(499)	(508)	9	-1.8%
Car hire and related fees	(716)	(619)	(97)	15.7%
Expense reimbursement and entertainment	(691)	(470)	(221)	47.0%
Membership fees	(257)	(219)	(38)	17.4%
Infoprovder expenses	(431)	(286)	(145)	50.7%
Special purpose vehicle expenses	(169)	-	(169)	n.a.
Maintenance of movables and real properties	(52)	(221)	169	-76.5%
Telephone and postage expenses	(182)	(184)	2	-1.1%
Stationery and printing	(109)	(57)	(52)	91.2%
Insurance	(207)	(67)	(140)	209.0%
Discretionary payments	(3)	(9)	6	-66.7%
Total	(20,907)	(20,112)	(795)	4.0%

Other administrative expenses increased by 4% compared to the previous year, primarily due to the combined effect of a reduction in servicing costs that more than offset the increases in consultancy costs. The figure at 31 December 2016 includes administrative expenses attributable to Beta of €641 thousand.

In particular, costs related to collection and servicing activities decreased as a result of the internalisation of the management of some portfolios that were previously managed externally and from a reduction in the cost percentage applied to managed collections.

The rise in computer expenses is linked to the increase in services provided by the outsourcer due to the increase in Group operations and IT updates on new products.

Consultancy costs increased due to the fact that part of the costs of projects correlated with new initiatives in 2016 were recognised during the period. In particular, the figure at 31 December 2016 includes €1.3 million of costs tied to the securitisation, €1.1 million of due diligence and consultancy costs relating to actual and potential acquisitions of new companies (of which €0.3 thousand related to the acquisition of Beta).

The other administrative expenses at 31 December 2016 were normalised and therefore do not include €0.3 million in costs related to the merger and integration of Beta

or the allocation of the extraordinary contribution to the National Resolution Fund of €1.3 million. In 2016, the other administrative expenses were normalised for costs related to the IPO of €2.4 million and the extraordinary contribution to the National Resolution Fund of €1.9 million.

The provision for risks and charges is primarily attributed to a prudent provision for a pending civil case against the Beta subsidiary.

Other expenses and income primarily consist of income deriving from the refund by the National Interbank Deposit Guarantee Fund of the sum of €290 thousand paid by the Bank in 2014 for the default of Banca Tercas, following the Bank's decision not to participate in the form of voluntary contribution described below. The item also includes €347 thousand for the 2016 contribution to the Deposit Guarantee Schemes.

Profit (loss) from equity investments includes not only the capital gain on the sale of 15.8% of the interest in CS Union, but also the pro-rata loss for the period referring to the current 10% interest in CS Union.

The Group's tax rate decreased compared to the previous half-year, primarily due to the application of the participation exemption ("Pex") to the capital gain recorded on the sale of part of the interest in CS Union.

The following shows the reconciliation of the normalised and statutory income statement for 2016.

INCOME STATEMENT (€,'000)	31/12/2016 NORMALISED	NORMALISATION	31/12/2016 STATUTORY
Interest margin	71,000		71,000
Net fee and commission income	9,060		9,060
Dividends and similar income	227		227
Profit (Loss) on trading	(84)		(84)
Profit from disposal or repurchase of financial assets	1,280		1,280
Net interest and other banking income	81,483		81,483
Net value adjustments due to loan impairment	(9,765)		(9,765)
Net income from banking activities	71,718		71,718
Personnel expenses	(15,169)		(15,169)
Other administrative expenses	(20,907)	(1,622)	(22,529)
Net allowance for risks and charges	(431)		(431)
Net value adjustments to property and equipment/intangible assets	(308)		(308)
Other operating income (expenses)	150		150
Operating expenses	(36,665)	(1,622)	(38,287)
Profit (loss) from equity investments	2,281		2,281
Profit (Loss) from disposal of investments	0		0
Profit from current operations before taxes	37,334	(1,622)	35,712
Income taxes for the period	(10,926)	527	(10,399)
Profit (loss) for the period	26,408	(1,095)	25,313

The normalisation of other administrative expenses refer to the extraordinary contribution to the National Resolution Fund for €1.3 million and costs related to the integration of Beta for €0.3 million.

The following shows the reconciliation of the normalised and statutory income statement for 2015.

INCOME STATEMENT (€,000)	2015 NORMALISED	IPO COSTS	FUND RESOLUTION	2015 STATUTORY
Interest margin	58,006	-		58,006
Net fee and commission income	11,168	-		11,168
Profit (Loss) on trading	122	-		122
Profit from disposal or repurchase of financial assets	2,518	-		2,518
Net interest and other banking income	71,814	-		71,814
Net value adjustments due to loan impairment	(5,439)	-		(5,439)
Net income from banking activities	66,375	-		66,375
Personnel expenses	(13,139)	(4,389)		(17,528)
Other administrative expenses	(20,112)	(2,386)	(1,852)	(24,350)
Net allowance for risks and charges				
Net value adjustments to property and equipment/ intangible assets	300 (312)	- -		300 (312)
Other operating income (expenses)	71	-		71
Operating expenses	(33,192)	(6,775)	(1,852)	(41,819)
Profit (loss) from equity investments	422	-		422
Profit (Loss) from disposal of investments	534	-		534
Profit from current operations before taxes	34,139	(6,775)	(1,852)	25,512
Income taxes for the period	(10,426)	1,919	602	(7,905)
Profit (loss) for the period	23,713	(4,856)	(1,250)	17,607

Personnel expenses include a gross variable component recognised to the management and linked to the Bank's listing.

The other administrative expenses mainly include share

placement commissions, consultancy costs and other costs linked to the listing process.

The sum of €1.9 million comprises the extraordinary contribution to the National Resolution Fund.

Beta's results

This section contains commentary on the results of Beta, the Group's most significant equity investment, which have been reclassified according to the presentation for banks.

The income statement table includes a column with the results for the second half of 2016, which represents the amount contributed to the Group's income statement results.

STATEMENT OF FINANCIAL POSITION ASSETS

(In thousands of Euro)

	31/12/2016	31/12/2015
Cash and cash equivalents	2	2
Due from banks	14,362	28,765
Loans to customers	68,555	76,815
Property and equipment	31	96
Intangible assets	14	24
Tax assets	4,020	2,457
Other assets	1,251	1,600
Total assets	88,235	109,759

STATEMENT OF FINANCIAL POSITION - LIABILITIES

(In thousands of Euro)

	31/12/2016	31/12/2015
Due to banks	-	-
Due to customers	19,575	23,199
Securities issued	-	16,175
Tax liabilities	4,968	5,231
Other liabilities	1,471	3,056
Employee termination indemnities	358	414
Reserves	12,069	11,882
Share capital	47,000	47,000
Profit (loss) for the year (+/-)	2,387	2,802
Total liabilities and shareholders' equity	88,235	109,759

(Amounts in thousands of Euro)	31/12/2016	31/12/2015	01/07/2016 - 31/12/2016
Interest and similar income	5,328	5,132	2,615
Interest expense and similar expense	(516)	(1,594)	(9)
Interest margin	4,812	3,538	2,606
Fee and commission income	946	1,275	436
Fee and commission expense	-	-	-
Net fee and commission Income	946	1,275	436
Net Interest and other banking Income	5,758	4,813	3,042
Value adjustments/write-backs due to impairment of:	821	3,113	(58)
a) receivables	821	3,113	(58)
Net Income from banking activities	6,579	7,926	2,984
Administrative expenses:	(3,047)	(3,684)	(1,283)
a) personnel expenses	(1,633)	(1,972)	(642)
b) other administrative expenses	(1,414)	(1,712)	(641)
Net adjustments to/recoveries on property and equipment	(13)	(32)	(1)
Net adjustments to/recoveries on intangible assets	(17)	(54)	(7)
Other operating income (expenses)	(55)	(84)	(75)
Operating expenses	(3,632)	(3,854)	(1,866)
Profit (loss) before tax from continuing operations	2,947	4,072	1,118
Taxes on income from continuing operations	(559)	(1,270)	(178)
Profit (loss) for the year	2,388	2,802	940

The positive change in interest margins is tied to the significant reduction in funding interest resulting from the Company's full repayment during the period, to the (former) single shareholder, of the subordinated loan using its own available funds. With respect to interest income: late payment interest from debtors (without-recourse operations) remained stable, interest earned from customers on with-recourse advances increased,

while interest on bank deposits decreased because of the reduction in the bank balance following the repayment of the subordinated loan mentioned previously.

Fixed costs declined considerably compared to the previous year due to the reduction in headcount.

Net profit was positively impacted by lower taxes resulting from the application of the ACE ("Assistance for economic growth") provision.

RISK MANAGEMENT AND SUPPORT CONTROL METHODS

With reference to the functioning of the “Risk Management System”, the Bank has adopted a system based on four leading principles:

- suitable supervision by relevant company bodies and functions;
- suitable policies and procedures to manage risks (both in terms of credit risk and the granting of loans);
- suitable methods and instruments to identify, monitor and manage risks, with suitable measuring techniques;
- thorough internal controls and independent audit.

The ‘Risk Management System’ is monitored by the Risk department, which ensures that capital adequacy and the degree of solvency with respect to its business are kept under constant control.

Management continuously analyses the Bank’s operations to fully identify the risks the Bank is exposed to (risk map).

To reinforce its ability to manage corporate risks, the Bank has set up a Risk Management Committee and ALM, whose mission is to help the Bank define strategies, risk policies, and profitability and liquidity targets.

The Risk Management Committee and ALM continuously monitor relevant risks and any new or potential risks arising from changes in the working environment or scheduled Group operations.

Pursuant to the eleventh amendment of Bank of Italy Circular 285/13, within the framework of the Internal Control System (Part I, Section IV, Chapter 3, Subsection II, Paragraph 5) the Bank entrusted the Internal Control Committee and Risk Management with the task of coordinating the second and third level Control Departments; to that end, the Committee allows the integration and interaction between these Departments, encouraging cooperation, reducing overlaps and supervising operations.

During the year, the Bank modified its second level control structure by separating the Compliance Department from the Risk Management Department, and assigning the head of the new department the role

of Compliance Officer.

With reference to the risk management framework, the Bank adopts an integrated reference framework both to identify its own risk appetite and for the internal process of determining capital adequacy. This system is the Risk Appetite Framework (RAF), designed to make sure that the growth and development aims of the Bank are compatible with capital and financial solidity.

The RAF comprises monitoring and alert mechanisms and related processes to take action in order to promptly intervene in the event of discrepancies with defined targets. The framework is subject to annual review based on the strategic guidelines and regulatory changes.

The ICAAP (the Internal Capital Adequacy Assessment Process) allows the Bank to conduct ongoing tests of its structure for determining risks and to update the related safeguards included in its RAF.

With regard to protecting against credit risk, along with the well-established first level controls and the periodic monitoring put in place by the Risk Management Department, the Bank is completing a process related to a valuation model for the provision for bad loans deriving from Public Administration debtors on Factoring products.

The main assumption of this model is the absence of credit risk for PA debtors through the allocation of a provision for each invoice once the expected collection date has passed, that is, the end of the discount period, and is based on the actual value of expected future cash flows, taking into account the recovery times. The analysis is expected to be concluded in the first half of 2017.

With regard to the monitoring of credit risk, the Bank (beginning in April 2016) has a dedicated collection department (Collection Department) which reports directly to the CEO and whose operations are regulated by a specific internal policy.

It should also be noted that, in accordance with the obligations imposed by the applicable regulations, each year the Bank publishes its report (Pillar 3) on capital

adequacy, risk exposure and the general characteristics of the systems for identifying, measuring and managing risks. The report is available on the website www.bancasistema.it in the Investor Relations section.

In order to measure 'Pillar 1 risks', the Group has adopted standard methods to calculate the capital requirements for Prudential Regulatory purposes. In order to evaluate

"Pillar 2" risks, the Bank adopts - where possible - the methods set out in the Regulatory framework or those established by trade associations.

If there are no such indications, standard market practices by operators working at a level of complexity and with operations comparable to those of the Bank are assessed.

New regulatory and tax provisions

BRRD (Bank Recovery and Resolution Directive - 2014/59/EU)

The BRRD (the Bank Recovery and Resolution Directive - 2014/59/EU) established new resolution rules, applicable from 1 January 2015 to all banks in the European Union, and its measures are financed, with effect from 1 January 2015, by the National Resolution Fund, which, with effect from 1 January 2016, was merged into the Single Resolution Fund (SRF). In fact, with effect from that date, the national funds of all countries belonging to the monetary union, instituted in 2015 in accordance with the BRRD, were merged into the Single Resolution Fund. On 29 April 2016, with subsequent ratification on 27 May 2016, the Bank of Italy, as the resolution authority, gave notice of the ordinary contribution due

for 2016, calculated in accordance with Commission Delegated Regulations 2015/63 and 2015/81. As at 30 June 2016, in application of IFRIC 21 Levies, the Bank recognised the full contribution of €655 thousand (€617 thousand in 2015) in the income statement, under other administrative expenses. The Bank of Italy, through the Communication dated 27 December 2016, called for two years of additional contributions for 2016 pursuant to art. 1, paragraph 848, of Law no. 208 of 28 December 2015, given art. 25 of Law Decree no. 237 of 23 December 2016. The amount of the extraordinary contribution, which was fully accounted for in the 2016 income statement, was €1.3 million.

DGS (Deposit Guarantee Schemes) Directive (former National Interbank Deposit Guarantee Fund)

The publication in the Official Journal of the Italian Republic no. 56 of 8 March 2016 of Legislative Decree no. 30 of 15 February 2016 marked the transposition of the DGS Directive (Deposit Guarantee Schemes - 2014/49/EU), aimed at increasing the protection of depositors and harmonising the regulatory framework at the European level. The calculation criteria, and thus the amount of the contribution for 2016, have yet to be defined.

As at 31 December 2015, an additional mechanism beyond that governed by the DGS Directive was in place on a voluntary basis (the "Voluntary Scheme"), with the

aim of supporting banks under receivership or in distress, in which the Group elected not to participate. The Bank began to operate in late 2011 and thus decided not to contribute to losses deriving from events that occurred prior to the Bank's existence. Accordingly, on 26 April 2016 the National Interbank Deposit Guarantee Fund gave notice of the refund of the contribution previously paid for Banca Tercas (which the European Commission considered as "state aid") of €290 thousand, recognised in the income statement under other operating income. The amount of the contribution for 2016 was €347 thousand.

New Contracting Code

The text of the new Contracting Code (Legislative Decree no. 50 of 18 April 2016) was published in Italy's Official Journal on 19 April 2016. Article 106 (13) of the Code reads as follows:

"13. The provisions of Law no. 52 of 21 February 1991 shall apply. To be enforceable on contracting authorities, the assignment of receivables must be witnessed by a public deed or authenticated private agreement and the debtor administrations must be notified. Without prejudice to the observance of traceability obligations, assignment of receivables deriving from consideration for tenders, concessions and planning competitions is valid and binding on contracting authorities that are public administrations if such administrations do not

reject them with notice to be served on the assignor and assignee within 45 days of notice of assignment. In the contract entered into or in a concurrent separate agreement, public administrations may accept in advance the assignment by the performing party of all or part of the receivables that have yet to accrue. In any event, the entity that has been notified of the assignment may raise all objections against the assignee that were available to the assignor under the contract governing works, services, the supply of goods or design entered into with the latter."

The new statute does not substantially modify the rules previously set out in Article 117 of the repealed Contracting Code (Legislative Decree no. 163/2006).

OTHER INFORMATION

Report on governance and ownership

Pursuant to art. 123-bis, paragraph 3 of Legislative Decree no. 58 dated 24 February 1998, a "Report on governance and ownership" has been drawn up; the document - published jointly with the draft Financial Statements for the FY ended 31 December 2016 - is available in the Governance Section of the Bank website (www.bancasistema.it).

Remuneration Report

Pursuant to art. 84-quater, paragraph 1 of

Legislative Decree no. 58 dated 24 February 1998, a "Remuneration Report" has been drawn up; the document - published jointly with the draft Financial Statements for the FY ended 31 December 2016 - is available in the Governance Section of the Bank website (www.bancasistema.it).

Research and Development Activities

No research and development activity was carried out in 2016.

TRANSACTIONS WITH RELATED PARTIES

Transactions with related parties and connected parties, including the relative authorisation and disclosure procedures, are governed by the 'Procedure governing transactions with associated parties' approved by the Board of Directors and published on the internet site of the Parent Company, Banca Sistema S.p.A..

Transactions between the Group companies and related parties or connected parties were carried out in the interests of the Bank, including within the scope of ordinary operations; these transactions were carried out in accordance

with market conditions and, in any event, based on mutual financial advantage and in compliance with all procedures.

With respect to transactions with parties who exercise management and control functions in accordance with art. 136 of the Consolidated Law on Banking, they are included in the Executive Committee resolution, specifically authorised by the Board of Directors and with the approval of the Statutory Auditors, subject to compliance with the obligations provided under the Italian Civil Code with respect to matters relating to the conflict of interest of directors.

ATYPICAL OR UNUSUAL TRANSACTIONS

During 2016, the Group did not carry out any atypical or unusual transactions, as defined in Consob Communication no. 6064293 of 28 July 2006.

SIGNIFICANT EVENTS AFTER THE END OF THE PERIOD

During the month of January, the inspection initiated by the Bank of Italy in October 2016 was concluded. The outcome of the inspection is expected during the first or second quarter of 2017.

The migration and integration connected to the merger by

incorporation of Beta Stepstone into the Parent Company were completed with legal and tax effect beginning on 1 January 2017.

There were no additional significant events after the end of the period to be mentioned.

BUSINESS OUTLOOK AND MAIN RISKS AND UNCERTAINTIES

The 2016 financial year ended with continuing growth in volumes and revenues in the factoring sector and in terms of salary-backed loans (CQS).

Particularly in factoring, the commercial agreements entered into in 2015 have contributed to the Group's growth and product and customer diversification process, much like the way the Beta acquisition will provide an increased ability to manage Collection/Servicing of loans

in legal action to a Group level.

The objective for the following year is to consolidate growth in the core factoring business and to take advantage of additional growth opportunities in salary-backed loans (CQS). The reduced focus on guaranteed loans to SMEs will be compensated by new product lines and the evaluation of strategic and complementary acquisitions.

Milano, 8 March 2017

On behalf of the Board of Directors

The Chairman
Luitgard Spögler

The CEO
Gianluca Garbi

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

(Amounts in thousands of Euro)

Assets		31/12/2016	31/12/2015
10.	Cash and cash equivalents	98	104
20.	Financial assets held for trading	996	-
40.	Financial assets available for sale	514,838	925,402
60.	Due from banks	83,493	2,076
70.	Loans to customers	1,348,329	1,457,990
100.	Equity investments	1,030	2,696
120.	Property and equipment	23,313	1,058
130.	Intangible assets	1,835	1,872
	of which goodwill	1,786	1,786
140.	Tax assets	10,528	7,353
	a) current	3,034	3,537
	b) deferred	7,494	3,816
	b1) as specified in Law 214/2011	3,984	2,658
160.	Other assets	14,903	13,119
	Total assets	1,999,363	2,411,670

(Amounts in thousands of Euro)

Voci del passivo e del patrimonio netto		31/12/2016	31/12/2015
10.	Due to banks	458,126	362,075
20.	Due to customers	1,262,123	1,878,339
30.	Securities issued	90,330	20,102
80.	Tax liabilities	8,539	804
	a) current	1,076	-
	b) deferred	7,463	804
100.	Other liabilities	59,825	55,317
110.	Employee termination indemnities	1,998	1,303
120.	Provisions for risks and charges	4,105	372
	b) other provisions	4,105	372
140.	Valuation reserves	425	350
170.	Reserves	39,608	26,314
180.	Share premium reserve	39,352	39,436
190.	Share capital	9,651	9,651
200.	Treasury shares (-)	(52)	-
210.	Minority interests	20	-
220.	Profit (loss) for the year	25,313	17,607
	Total liabilities and shareholders' equity	1,999,363	2,411,670

CONSOLIDATED INCOME STATEMENT

(Amounts in thousands of Euro)

Items	31/12/2016	31/12/2015
10. Interest and similar income	86,321	79,019
20. Interest expense and similar expense	(15,321)	(21,013)
30. Interest margin	71,000	58,006
40. Fee and commission income	10,895	12,742
50. Fee and commission expense	(1,835)	(1,574)
60. Net fee and commission income	9,060	11,168
70. Dividends and similar income	227	-
80. Profit (Loss) on trading	(84)	122
100. Profit (loss) from disposal or repurchase of:	1,280	2,518
b) financial assets available for sale	1,280	2,518
120. Net interest and other banking income	81,483	71,814
130. Net value adjustments/write-backs due to impairment of:	(9,765)	(5,439)
a) receivables	(9,765)	(5,439)
140. Net income from banking activities	71,718	66,375
180. Administrative expenses:	(37,698)	(41,878)
a) personnel expenses	(15,169)	(17,528)
b) other administrative expenses	(22,529)	(24,350)
190. Net allowance for risks and charges	(431)	300
200. Net adjustments to/recoveries on property and equipment	(250)	(252)
210. Net adjustments to/recoveries on intangible assets	(58)	(60)
220. Other operating income (expenses)	150	71
230. Operating expenses	(38,287)	(41,819)
240. Profit (loss) from equity investments	2,281	422
270. Profit (Loss) from disposal of investments	-	534
280. Profit (loss) before tax from continuing operations	35,712	25,512
290. Taxes on income from continuing operations	(10,399)	(7,905)
300. Profit (loss) after tax from continuing operations	25,313	17,607
320. Profit (loss) for the year	25,313	17,607
340. Parent company profit for the year	25,313	17,607

CONSOLIDATED STATEMENT OF OTHER COMPREHENSIVE INCOME

(Amounts in thousands of Euro)

Items		31/12/2016	31/12/2015
10.	Profit (loss) for the year	25,313	17,607
	Other income items net of taxes without reversal to the income statement		
40.	Defined benefit plans	(56)	(46)
	Other income items net of taxes with reversal to the income statement	-	-
100.	Financial assets available for sale	263	394
130.	Total other comprehensive income (net of tax)	207	348
140.	Comprehensive income (Items 10+130)	25,520	17,955
150.	Total consolidated comprehensive income pertaining to minority interests	-	-
160.	Total consolidated comprehensive income pertaining to the Parent Company	25,520	17,955

STATEMENTS OF CHANGES IN CONSOLIDATED EQUITY AS AT 31/12/2016

Amounts in thousands of Euro

	Balance at 31.12.2015	Change in opening balances	Balance at 01.01.2016	Allocation of net result from pre-vi-ous year		Changes during the year										Group shareholders' equity at 31.12.2016	Minority shareholders' equity at 31.12.2016		
				Reserves	Dividends and other allocations	Changes in reserves	Issue of new shares	Purchase of treasury shares	Extraordinary dividends	Changes in equity instruments	Derivatives on treasury shares	Stock Options	Changes in equity investments	Comprehensive income as at 31.12.2016					
Share capital:																			
a) ordinary shares	9,651	-	9,651														9,651	20	
b) other shares	-	-	-														-	-	
Share premium reserve	39,436	-	39,436			(84)											39,352	-	
Reserves	26,314	-	26,314	13,345	-	(50)											39,608	-	
a) retained earnings	26,573	-	26,573	13,345	-	-											39,918	-	
b) other	(259)	-	(260)			(50)											(310)	-	
Valuation reserves	350	-	350			(131)											425	-	
Equity instruments	-	-	-														-	-	
Treasury shares	-	-	-					(52)									(52)	-	
Profit (loss) for the period	17,607	-	17,607	(13,345)	(4,262)	-											25,313	-	
Group shareholders' equity	93,358	-	93,358	-	-	(134)											25,520	114,296	-
Minority shareholders' equity	-	-	-			20											-	20	

STATEMENT OF CHANGES IN CONSOLIDATED EQUITY AS AT 31/12/2015

Amounts in thousands of Euro

	Balance at 31.12.2014	Change in opening balances	Balance at 01.01.2015	Allocation of net result from previous year		Changes during the year							Comprehensive income as at 31.12.2015	Group shareholders' equity at 31.12.2015		
				Reserves	Dividends and other allocations	Changes in reserves	Issue of new shares	Purchase of treasury shares	Extraordinary distribution - dividends	Changes in equity instruments	Derivatives on treasury shares	Stock Options			Changes in equity investments	
Share capital:																
a) ordinary shares	8,451	-	8,451	-	-	1,200	-	-	-	-	-	-	-	-	-	9,651
b) other shares		-		-	-	-	-	-	-	-	-	-	-	-	-	-
Share premium reserve	4,325	-	4,325	-	-	35,111	-	-	-	-	-	-	-	-	-	39,436
Reserves	8,734	-	8,734	17,567	-	13	-	-	-	-	-	-	-	-	-	26,314
a) retained earnings	9,006	-	9,006	17,567	-	-	-	-	-	-	-	-	-	-	-	26,573
b) other	(272)	-	(272)	-	-	13	-	-	-	-	-	-	-	-	-	(259)
Valuation reserves	2	-	2	-	-	-	-	-	-	-	-	-	-	-	348	350
Equity instruments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Treasury shares	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Profit (loss) for the period	19,539	-	19,539	(17,567)	(1,972)	-	-	-	-	-	-	-	-	-	17,607	17,607
Shareholders' equity	41,051	-	41,051	-	(1,972)	36,324	-	-	-	-	-	-	-	-	17,955	93,358

CONSOLIDATED STATEMENT OF CASH FLOWS (direct method)

Amounts in thousands of Euro

	31/12/2016	31/12/2015
A. OPERATING ACTIVITIES		
1. Operations	29,701	12,997
▪ interest income collected	86,321	79,019
▪ interest expense paid	(15,321)	(21,013)
▪ net fees and commissions	9,060	11,168
▪ personnel expenses	(13,518)	(15,848)
▪ other expenses	(22,810)	(23,978)
▪ taxes and duties	(14,031)	(16,351)
2. Cash flows generated by (used in) financial assets	429,438	(323,797)
▪ financial assets held for trading	(1,080)	185
▪ financial assets available for sale	411,919	(64,529)
▪ loans to customers	99,896	(269,675)
▪ due from banks: on demand	(81,397)	14,606
▪ other assets	100	(4,384)
3. Cash flows generated by (used in) financial liabilities	(434,916)	276,429
▪ due to banks: on demand	96,051	(459,329)
▪ due to customers	(616,216)	724,542
▪ securities issued	70,228	(7)
▪ other liabilities	15,021	11,223
Net cash flow generated by (used in) operating activities	24,223	(34,371)
B. INVESTMENT ACTIVITIES		
1. Cash flows from	2,610	-
▪ sales of equity investments	2,383	-
▪ dividends collected on equity investments	227	-
2. Cash flows used in	(22,526)	(137)
▪ purchases of property and equipment	(22,505)	(109)
▪ purchases of intangible assets	(21)	(28)
▪ purchases of subsidiaries and business lines	-	-
Net cash flow generated by (used in) investment activities	(19,916)	(137)
C. FINANCING ACTIVITIES		
▪ issues/purchases of treasury shares	(52)	36,517
▪ issues/purchases of equity instruments	-	-
▪ dividend distribution and other	(4,261)	(1,972)
Net cash flow generated by (used in) financing activities	(4,313)	34,545
NET CASH FLOW GENERATED/USED DURING THE YEAR	(6)	38

Items

RECONCILIATION

Cash and cash equivalents at the beginning of the year	104	66
Total net cash flow generated/used during the year	(6)	38
Cash and cash equivalents at balance sheet date	98	104

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

A.1 - GENERAL PART

SECTION 1 - Statement of compliance with international accounting standards

The Consolidated financial statements of the Banca Sistema S.p.A. Group as at 31 December 2016 were drawn up in accordance with International accounting standards - called IAS/IFRS - issued by the International Accounting Standards Board (IASB) and interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and approved by the European Commission, as established by EU Regulation no. 1606 of 19 July 2002, adopted in Italy by art. 1 of Legislative Decree no. 38 of 28 February 2005 and considering circular by the Bank of Italy no. 262 of 22 December 2005 as subsequently updated, regarding the forms and rules for drafting the Banks' Financial Statements.

The International Accounting Standards are applied by referring to the "Systematic Framework for preparing and presenting Financial Statements" (Framework).

If there is no standard or interpretation that applies specifically to a transaction, other event or circumstance, the Board of Directors uses its judgement to develop and apply an accounting standard in order to provide disclosure that:

- is relevant to the purposes of the financial decisions made by the users;
- reliable, so that the consolidated financial statements:
 - faithfully represent the capital/financial position, the profit and loss and the cash flows of the entity;
 - reflect the economic substance of the operations, other events and circumstances and not merely the legal form;
 - are neutral, i.e. devoid of prejudice;
 - are prudent;
 - are complete, with reference to all relevant aspects.

When exercising the aforementioned judgement, the Board of Directors of the Bank has made reference to and considered the applicability of the following sources, described in descending order of importance:

- the provisions and application guidelines contained in the Principles and Interpretations governing similar or related cases;
- the definitions, recognition criteria and measuring concepts for accounting for the assets, liabilities, revenues, and costs contained in the "Systematic framework".

When expressing an opinion, the Board of Directors may also consider the most recent provisions issued by other bodies that rule on accounting standards that use a "Systematic framework" similar in concept to developing accounting standards, other accounting literature and consolidated practices in the sector.

In accordance with art. 5 of Legislative Decree no. 38 of 28 February 2005, if, in exceptional cases, the application of a provision imposed by the international accounting standards were incompatible with the true and correct representation of the capital or financial position or the profit and loss result, the provision would not apply. The justifications for any exceptions and their influence on the representation of the capital situation or financial position or profit and loss would be explained in the Notes to the financial statements. Any profits resulting from the exception would be recorded in a non-distributable reserve if they did not correspond to the recovered value in the financial statements. However, no exceptions to the IAS/IFRS were applied. The financial statements were audited by KPMG S.p.A..

SECTION 2 - General accounting policies

The Financial Statements are drawn up with clarity and are a true and faithful representation of the capital and financial position and the profit and loss for the year, the changes in equity and the cash flows and comprise the statement of financial position, the income statement,

statement of comprehensive income, the statement of changes in equity, the cash flow statement, and the notes to the financial statements.

The Financial Statements are accompanied by the Director's Report on Management Performance.

If the information required by the international accounting principles and provisions contained in Circular no. 262 of 22 December 2005 and/or the subsequent updates issued by the Bank of Italy is not sufficient to give a true and correct representation that is relevant, reliable, comparable, and understandable, the explanatory notes provide the additional information required.

The general principles that underlie the drafting of the financial statements are set out below:

- the measurements are made considering that the company will continue as an ongoing business guaranteed by the financial support of the Shareholders;
- costs and revenue are accounted for on an accrual basis;
- to ensure the comparability of the data and information in the financial statements and the notes to the financial statements, the methods of representation and classification are kept constant over time unless they are changed to present the data more appropriately;
- each significant class of similar items is separately indicated in the statement of financial position and income statement; items with dissimilar natures or uses are presented separately unless they are considered to be irrelevant;
- accounts that have no associated sums for the financial year or for the previous financial year are not indicated in the in the statement of financial position and income statement;
- if an element of the assets or liabilities comes under several items in the statement of financial position, the notes to the financial statements make reference to the other items under which it is recorded if it is necessary for a better understanding of the financial statements;
- the items are not offset against one another unless it is expressly requested or allowed by an international

accounting standard or an interpretation or the provisions of the aforementioned Circular no. 262 of 22 December 2005 as amended by the Bank of Italy;

- the financial statements are drafted by favouring substance over form and in accordance with the principle of relevance and significance of the information;
- comparative data for the previous financial year are presented for each account of the statement of financial position and income statement; if the accounts are not comparable to those of the previous year, they are adapted and the non-comparability and adjustment/or impossibility thereof are indicated and commented on in the notes to the financial statements;
- the layout recommended by the Bank of Italy was used with reference to the information reported in the notes to the financial statements; they were not presented if they were not applicable to the Bank's business.

Within the scope of drawing up the financial statements in accordance with the IAS/IFRS, company management must make assessments, estimates and assumptions that influence the amounts of the assets, liabilities, costs and returns for the period.

As provided in IAS 8, it is essential to make reasonable estimates when preparing the financial statements. The estimates that had to be made when drawing up these financial statements do not adversely affect their reliability; these estimates are regularly revised and are mainly based on previous experience.

Any changes resulting from the review of the accounting estimates are reported in the period in which the revision is made if it relates only to that period. If the revision relates to either current or future periods, the change is reported in the period in which the revision is made and in the relevant future periods.

Pursuant to the provisions of art. 5 of Legislative Decree no. 38 of 28 February 2005, the financial statements use the Euro as the currency for accounting purposes. Amounts presented in the financial statements are in thousands of Euro.

Note the following in reference to regulatory developments in the IAS/IFRS international accounting standards:

Regulations (EU)	Stock performance
2015/28 of 17 December 2014	IFRS Annual Improvements Cycle 2010-2012 - IFRS 2, 3 and 8 and IAS 16, 24 and 38
2015/29 of 17 December 2014	Changes to IAS 19
2015/2113 of 23 November 2015	Changes to IAS 16 and 41
2015/2173 of 24 November 2015	Changes to IFRS 11
2015/2231 of 2 December 2015	Changes to IAS 16 and 38
2015/2343 of 15 December 2015	Changes to IFRS 5 and 7 and IAS 19 and 34
2015/2406 of 18 December 2015	Changes to IAS 1
2015/2441 of 18 December 2015	Changes to IAS 27
2016/1703 of 22 September 2016	Changes to IFRS 10, IFRS 12 and to IAS 28

The new international accounting principles that take effect on 1 January 2018 are reported in the table below.

Regulations (EU)	Stock performance
2016/1905 of 22 September 2016	IFRS 15 - Revenue from Contracts with Customers
2016/2067 of 22 November 2016	IFRS 9 - Financial instruments

SECTION 3 - Area and methods of consolidation

The consolidated financial statements include the Parent Company Banca Sistema S.p.A. and the companies directly or indirectly controlled by or connected with it.

The following statement shows the investments included within the scope of consolidation of the consolidated report.

Company Names	Registered office	Type of relationship (1)	Investment		
			Investing company	% held	% of votes available (2)
Companies					
Companies subject to full consolidation					
S.F. Trust Holdings Ltd	London	1	Banca Sistema	100%	100%
Beta Stepstone S.p.A.	Italy	1	Banca Sistema	100%	100%
Largo Augusto Servizi e Sviluppo S.r.l.	Italy	1	Banca Sistema	100%	100%
Consolidated at equity					
C.S. Union S.p.A.	Italy	4	Banca Sistema	10%	10%

Changes in the scope of consolidation

Compared to the situation as at 31 December 2015, the scope of consolidation changed due to the inclusion of Beta Stepstone S.p.A. (acquired on 1 July 2016) and Largo Augusto Servizi e Sviluppo S.r.l. (established on 25 August 2016), both of which are wholly owned by the Parent company.

Full consolidation method

The investments in subsidiaries are consolidated using the full consolidation method. The concept of control goes beyond owning a majority of the percentage of stakes in the share capital of the subsidiary and is defined as the power of determining the management and financial policies of the said subsidiary to obtain

benefits from its business.

Full consolidation provides for line-by-line aggregation of the balance sheet and income statement aggregates from the accounts of the subsidiaries. To this end, the following adjustments were made:

- (a) the book value of the investments held by the Parent Company and the corresponding part of the shareholders' equity are eliminated;
- (b) the portion of shareholders' equity and profit or loss for the year is shown in a specific caption.

The results of the above adjustments, if positive, are shown - after allocation to the assets or liabilities of the subsidiary - as goodwill in item '130 Intangible Assets' on the date of initial consolidation. The resulting differences, if negative, are recognised in the income statement. Intra-group balances and transactions, including revenue, costs and dividends, are entirely eliminated. The financial results of a subsidiary acquired during the financial year are included in the consolidated financial statements from the date of acquisition. At the same time, the financial results of a transferred subsidiary are included in the consolidated financial statements up to the date on which the subsidiary is transferred. The accounts used in the preparation of the consolidated financial statements are drafted on the same date. The consolidated financial statements were drafted using consistent accounting standards for transactions and similar events. If a subsidiary uses accounting standards different from those adopted in the consolidated financial statements for transactions and events in similar circumstances, adjustments are made to the accounting position for consolidation purposes. Detailed information with reference to art. 89 of Directive 2013/36/EU of the European Parliament and Council (CRD IV) are published at the link www.bancasistema.it/pillar3.

Consolidation with the equity method

Associated companies are consolidated with the equity method.

The equity method provides for the initial recognition of the investment at cost and subsequent value adjustment

based on the relevant share of the shareholders' equity of the subsidiary.

The differences between the value of the equity investment and the shareholders' equity of the relevant subsidiary are included in the accounting value of the subsidiary.

In the valuation of the relevant share, any potential voting rights are not taken into consideration.

The relevant share of the annual results of the subsidiary is shown in a specific item of the consolidated income statement.

If there is evidence that the value of an equity investment may be impaired, the recoverable value of said equity investment is estimated by considering the present value of future cash flows that the investment could generate, including the final disposal value of the investment. Should the recovery value prove lower than the book value, the difference is recognised in the income statement.

SECTION 4 - Subsequent events

With regard to IAS 10, after 31 December 2016, the reference date of the consolidated financial statements, and up to 8 March 2017, the date that the financial statements were presented to the Board of Directors, no events occurred that would require any adjustments to the figures in the financial statements. On 1 March 2017, the branch located in Milan, via Vespri Siciliani, dedicated exclusively to collateralised loans, was opened. This activity was also recently started at the Bank's branch already in the city of Pisa.

SECTION 5 – Other aspects

Starting this financial year, the Bank revised its accounting treatment of late payment interest in accordance with IFRS as a result of the experience gained and the systematic implementation of out-of-court and judicial recovery measures for past-due receivables, and transitioned from cash accounting to accrual accounting only for receivables subject to legal action. The accounting was carried out based on the expected percentage of recovery which is at least 65% for debtors of the national health system, while for other PA debtors it is estimated to be at least 15%.

There are no significant aspects to note.

Changes to IAS 39

On 24 July 2014, the IASB completed its review process of IAS 39 by issuing IFRS 9 “Financial Instruments”, adoption of which is mandatory for financial years beginning on or after 1 January 2018. At the beginning of 2017, the Bank launched a project aimed at determining the qualitative and quantitative impacts on the financial statements, as well as to identify and subsequently implement the changes necessary at the organisational, internal regulation and application system levels. IFRS 9, which will replace IAS 39 “Financial Instruments: Recognition and Measurement”, introduces significant changes, particularly with regard to the following:

- Classification and measurement of financial instruments
- Impairment
- Hedge Accounting

With regard to classification and measurement activities, the Bank will perform a detailed review of the cash flow characteristics of instruments measured at amortised cost under IAS 39 to identify any assets that, not going beyond a SPPI (Solely Payments of Principal and Interest) review, should be valued at fair value according to IFRS 9.

From an initial assessment, the most significant and pervasive impacts are expected from implementing the new impairment model which transitions from the current “incurred loss” based model, to one based on the concept of “expected loss”.

A.2 - INFORMATION ON THE MAIN ITEMS OF THE FINANCIAL STATEMENTS

1. Financial assets held for trading

Classification criteria

This item classifies the financial instruments on a cash basis held for trading¹. A financial asset or liability is

classified as held-for-trading (so-called Fair Value Through Profit or Loss - FVPL), and recorded under line 20 “Held-for-trading financial assets” or line 40 “Held-for-trading financial liabilities”, if it is:

- purchased or held mainly to sell it or repurchase it in the short term;
- part of a portfolio of identified financial instruments managed on a single basis and where there is evidence of a recent and effective strategy aimed at obtaining profit in the short term;
- a derivative (apart from designated derivatives that are effective hedging instruments - see paragraph below on this issue).

Recognition criteria

Initial recognition of the held-for-trading financial assets occurs: I) at the settlement date for debt securities, capital and shares in UCITS; II) at the subscription date for derivative contracts.

The initial recognition of held-for-trading financial assets is at fair value, not including any transaction costs or income that are directly recognised on the income statement even though directly attributable to the instrument.

The initial fair value of a financial instrument is usually the cost incurred for its acquisition.

Measurement and recognition criteria for income components

Following initial recognition, held-for-trading financial assets are measured at fair value, and any changes are recorded in the income statement.

For more details on the methods of calculating the fair value please refer to paragraph 17.3 below “Criteria for calculating the fair value of financial instruments”.

Gains and losses on disposal or redemption and unrealised gains or losses resulting from changes in the fair value of held-for-trading financial assets are recognised in the income statement under “profit (loss) on trading”.

¹ The positions held for trading purposes are those that are meant to be subsequently transferred in the short term and/or held in order to provide short-term benefits in the difference between the purchase and the sales price or other price changes or interest rate changes. The positions are intended to mean own positions or positions resulting from Customer services or trading support (Market making).

Derecognition criteria

Held-for-trading financial assets are derecognised when the contractual rights on the cash flows deriving from the assets are lost, or in the case of a transfer, when the same entails the substantial transfer of all risks and benefits related to the assets.

2. Financial assets available for sale

Classification criteria

This category includes the non-derivative financial assets not classified otherwise as “Held-for-trading financial assets”, “Financial assets measured at fair value”, “Held-to-maturity financial assets” or “Receivables”.

The investments “available for sale” are financial assets that are intended to be retained for an indefinite period and that may be sold for reasons of liquidity, changes in interest rates, exchange rates or market prices.

A financial instrument is designated to the category in question when it is initially recorded or following any reclassifications in accordance with paragraphs 50 to 54 of IAS 39, as amended by Regulation (EC) no. 1004/2008 of the European Commission of 15 October 2008.

Recognition criteria

Initial recognition of available-for-sale financial assets is at the date of settlement, based on their fair value including the costs/income of the transaction directly attributable to the acquisition of the financial instrument. Costs/income having the previously mentioned characteristics that will be repaid by the debtor or that can be considered as standard internal administrative costs are excluded.

The initial fair value of a financial instrument is usually the cost incurred for its acquisition.

Measurement and recognition criteria for income components

Following initial recognition, available-for-sale financial assets are measured at their fair value with any gains or losses resulting from a change in the fair value compared to the amortised cost, recorded in a specific equity reserve recorded in the statement of comprehensive income up until said financial asset is derecognised or an impairment

loss is recorded.

For more details on the methods of calculating the fair value please refer to paragraph 17.3 below “Criteria for calculating the fair value of financial instruments”.

With reference to the valuation reserves relating to debt securities issued by the Central Authorities of countries belonging to the European Union, the Bank of Italy issued an order on 18 May 2010 recognising - for the purposes of calculating the regulatory capital (prudential filters) - the option of fully neutralising the capital gains and losses reported in the previously mentioned reserves after 31 December 2009. The Parent Company availed of that option starting from calculation of the regulatory capital.

Impairment testing is performed in accordance with paragraphs 58 et seq. of IAS 39 at every year-end. As regards equity securities listed on an active market, a significant or prolonged reduction of the fair value below the purchase cost is also evidence of impairment.

If the fair value is reduced in cost by more than 50% or in duration by more than 18 months, the impairment is considered to be permanent. If, however, the decrease in the fair value of the cost of the instrument is lower than or equal to 50% but above 20%, or in duration by not more than 18 months but not less than 9, the Group will analyse other income and market indicators. If the results of said analysis are such as to shed doubt on the possibility of recovering the amount originally invested, permanent impairment will be recognised. The amount transferred to the income statement is therefore equal to the difference between the book value (acquisition cost net of any losses due to impairment already reported in the income statement) and the current fair value.

The amount of any impairment is recorded under the income statement item “net value adjustments/write-backs due to impairment of available-for-sale financial assets”.

This amount also includes the reversal to the income statement of any profits/losses from the measurement previously recorded in the specific shareholders’ equity reserve. If, in a subsequent period, the fair value of the financial instrument increases and this increase may be objectively related to an event that occurred after the impairment was reported in the income statement, the impairment must be derecognised by reporting the write-

back under the same income statement item where monetary elements (for example, debt securities) and shareholders' equity if they relate to non-monetary items are reported (for example, equity securities). The write-back in the income statement may not, in any event, exceed the amortised cost that the instrument would have had in the absence of the previous adjustments.

Interest income on the aforesaid financial assets is calculated by applying effective interest rate criteria with recognition of the result under the income statement item "interest income and similar income".

The profits and losses deriving from the disposal or reimbursement of the aforementioned financial assets are reported in the income statement item "Profits (losses) from disposal or repurchase of: available-for-sale financial assets" and include the possible reversal to the income statement of the profits/losses previously recorded in the specific shareholders' equity reserve.

Derecognition criteria

Available-for-sale financial assets are derecognised when the contractual rights on the cash flows deriving from the assets expire, or in the case of a transfer, when the same entails the substantial transfer of all risks and benefits related to the financial assets.

3. Financial assets held to maturity

Held-to-maturity financial assets (HTM) are non-derivative financial assets, with fixed or calculable payments and fixed maturities for which there is the objective intention and capacity to hold them to maturity.

The following are not included:

- (a) those held for trading and those carried at fair value upon initial recognition recognised in the income statement (see paragraph 1: held-for-trading financial assets);
- (b) those designated as available for sale (see previous paragraph);
- (c) those that meet the definition of receivables and loans (see paragraph below).

When the financial statements or interim accounts are being drafted, the intention and capacity to hold financial assets to maturity is assessed.

These assets are reported under item "50 Held-to-maturity financial assets".

Recognition criteria

The held-to-maturity financial assets are initially reported when, and only when, the Group becomes party to the contractual clauses of the instrument, or at the time of settlement, at a value equal to the cost, inclusive of any directly attributable costs and income. If the reporting of this asset in this category derives from reclassification from the "Available-for-sale financial assets" or - only in rare circumstances if the asset is no longer owned for the purpose of selling or repurchasing it in the short term - by the "Held-for-trading financial assets", the fair value of the asset, recorded at the time of transfer, is taken as the new measurement of the amortised cost of this asset.

Measurement criteria

The held-to-maturity financial assets are valued at the amortised cost, using the effective interest rate method (for a definition of this, please refer to the paragraph below "Receivables and Loans"). The result from applying this method is charged to the income statement in item "10 Interest income and similar income".

Impairment testing of the assets is performed when drafting the financial statements or the interim reports. If there is impairment, the difference between the book value of the asset and the current value of the estimated future cash flows, discounted at the original effective interest rate, is charged to the income statement under "130 Net value adjustments/write-backs due to impairment of c) held-to-maturity financial assets". The same income statement item also reports any write-backs recorded if the reasons behind the previous value adjustments are no longer valid. The fair value of the held-to-maturity financial assets is determined for information purposes or to ensure effective hedging against exchange risk or credit risk (in relation to the risk subject to hedging).

Derecognition criteria

Held-to-maturity financial assets are derecognised when the contractual rights on the cash flows deriving from the assets

are expired, or in the case of a transfer, when the same entails the substantial transfer of all risks and benefits related to the assets. The result of the disposal of the held-to-maturity financial assets is charged to the income statement under “100 Profits (losses) from the disposal or repurchase of c) held-to-maturity financial assets”.

4. Receivables

4.1. Due from banks

Classification criteria

This category includes cash financial assets held at banks that provide for fixed or calculable payments and are not listed on a market (current accounts, guarantee deposits, debt securities etc.).

It also includes amounts due from Central Banks that are not demand deposits (which are recorded under “Cash and cash equivalents”).

Please refer to paragraph 4.2 below “Loans to customers” for information regarding reporting, measurement, derecognition and recognition of the income items of the receivables.

4.2. Loans to customers

Classification criteria

Loans to customers include unstructured cash financial assets for customers that have fixed or calculable payments and that are not quoted on an active market.

Most loans to customers comprise on demand advances to customers as part of the factoring of non-recourse receivables acquired with respect to the Public Administration, where there are no contractual clauses that would prevent them from being registered. In accordance with the general principle of the precedence of economic substance over legal form, a company may cancel a financial asset from its financial statements only if it is through a transfer of the risks and benefits related to the transferred instrument. IAS 39 provides that a company can only cancel a financial asset from its financial statements if and only if:

- a) the financial asset is transferred and, with this, essentially all the risks and contractual rights to the cash flows deriving from the asset expire;

- b) the benefits attached to ownership of the asset are no longer valid.

The following conditions must be checked on an alternative basis in order for the financial asset to be transferred:

- a) the company has transferred the rights to receive cash flows from the financial asset;
- b) the company has maintained the right to receive the cash flows from the financial asset, but has assumed the obligation to pay them to one or more beneficiaries as part of an agreement in which the following conditions are met:
 - the company is under no obligation to pay predetermined sums to any beneficiary apart from what is received from the original financial asset;
 - the company may not sell or pledge the financial asset;
 - the company is under an obligation to transfer any financial flow that it collects, on behalf of any beneficiaries, without delay. Any investment of the financial flows for a period between cashing them and payment must take place only with financial assets that are equivalent to cash and therefore with no right to any interest that has matured on said invested sums.

In order to verify the transfer of a financial asset that results in the cancellation of the assignor from the financial statements, for each transfer the assigning company must assess the extent of any risks and benefits connected to the financial asset it holds.

In order to evaluate the actual transfer of the risks and benefits, the exposure of the assigning company must be compared with the variability of the current value or the financial flows generated by the financial asset transferred, before and after the assignment. The assigning company essentially maintains all the risks and benefits when its exposure to the “variability” of the current value of the net future financial flows does not change significantly following its transfer. However, there is a transfer when the exposure to this “variability” is no longer significant.

In summary, there can be three situations and each has specific effects, namely:

- a) if the company transfers almost all the risks and benefits of ownership of the financial asset, it

must 'write-off' the financial asset and record the rights or obligations deriving from the assignment separately as assets or liabilities;

- b) if the company maintains almost all the risks and benefits of ownership of the financial asset, it must continue to recognise the financial asset;
- c) if the company does not transfer or maintain almost all the risks and benefits of ownership of the financial asset, it must evaluate the elements of control of the financial asset, and:
 - if it does not have control, it must write off the financial asset and separately recognise the individual assets/liabilities resulting from the rights/obligations of the assignment;
 - if it maintains control, it must continue to recognise the financial asset up to the limit of its investment commitment.

In order to check control, the discriminating factor to consider is the beneficiary's capacity to unilaterally assign the financial asset without any restrictions by the assigning company. If the beneficiary of a financial asset transfer can sell the entire financial asset to a non-related third party and can do it unilaterally without having to impose any further limitations on the transfer, the assigning company no longer controls the financial asset. In all other cases, it maintains control over the financial asset.

The most frequently used forms of assigning a financial instrument may have profoundly different accounting effects:

- in the case of non-recourse transactions (with no guarantee restrictions), the assigned assets may be deleted from the assigning company's financial statements;
- in the case of a with-recourse assignment, in the majority of cases, the risk connected to the transferred asset remains with the seller and, therefore the assignment does not meet the requirements to have the instrument sold written off on an accounting basis.

Recognition criteria

Initial recognition of a receivable is at the date of settlement based on its fair value including the costs/income of the

transaction directly attributable to the acquisition of the receivable. Costs/income having the previously mentioned characteristics that will be repaid by the debtor or that can be considered as standard internal administrative costs are excluded.

The initial fair value of a financial instrument is usually equivalent to the amount granted or the cost incurred by the acquisition.

Measurement and recognition criteria for income components

Following initial recognition, loans to customers are stated at amortised cost, equal to the initial recognition value reduced/increased by capital repayments, by any value adjustments/write-backs and the amortisation – calculated based on the effective interest rate – of the difference between the amount provided and that repayable at maturity, usually the cost/income directly attributed to the individual loan.

The effective interest rate is the rate that discounts the flow of future payments estimated for the expected duration of the loan, in order to obtain the exact net book value at the time of initial recognition, which includes both the directly attributable transaction costs/income and all of the fees paid or received between the parties.

This accounting method, based on financial logic, enables the economic effect of costs/income to be spread over the expected residual life of the receivable.

The estimation of the flows and of the contractual duration of the loan considers all contractual clauses that may influence the amounts and the maturities (such as, for example, early extinction and various exercisable options), without considering, on the other hand, any losses expected on the loan.

Furthermore, an analysis is always performed to identify problem loans that show objective evidence of possible impairment at year-end. The methods used to calculate the analytical and generic write-downs applied to the credit portfolio are described below. In particular, exposures classified as impaired loans are analysed in order to quantify the potential impairment of the individual loan. With reference to the non-performing loans from the factoring portfolio with the Public Administration, the Bank

makes an analytical write-down for the Municipalities who are registered as having “financial difficulty” status in accordance with Legislative Decree 267/00.

If appropriate write-downs were not made at the pricing stage, the Bank makes an analytical write-down on the outstanding value of the loan net of the rediscount, which has not yet fallen due. The percentage write-down, without the Bank loss figures, was defined in accordance with the market benchmark.

On the other hand, with respect to the credit positions from the factoring portfolio where the debtor counterparty is a private company, the Bank does not record bad positions and therefore only applies a collective write-down to those positions.

For all the factoring portfolio credit positions that are classified as performing and past due (Public Administration and private), the Bank makes a prudential write-down, defining a segment of the portfolio through specific clusters defined when acquiring the portfolios and for which it makes in-depth assessments at the pricing stage, and therefore on those types of receivables and also exposures to Central Administration offices (for example Ministries). On the other hand, with respect to the exposures related to ordinary factoring receivables, a generic write-down was applied by applying a fixed percentage to the factoring portfolio.

With reference to the impaired loans forming part of the SME portfolio, the Group writes-down the entire portion of the loan that is not backed by the Guarantee Fund issued by Mediocredito Centrale.

With respect to performing SME loans, the Group defined a generic write-down in accordance with the percentage of impaired income observed on its portfolio.

With respect to the pension and salary-backed loans, since no non-performing positions have been recorded, the Group wrote-down the receivables based on market benchmarks.

Derecognition criteria

Loans are derecognised from the financial statements when they are deemed totally unrecoverable or if transferred, when this entails the substantial transfer of all loan-related risks and benefits.

5. Financial assets at fair value through profit and loss

At the date of the financial statements, the company did not hold any “Financial assets measured at fair value”.

6. Hedging transactions

At the date of the financial statements, the Company had not made any “Hedging transactions”.

7. Equity investments

Classification criteria

This category includes investments in subsidiaries, associates, and joint ventures by Banca Sistema.

Recognition criteria

Equity investments are recorded in the financial statements at purchase cost.

Measurement criteria

The equity method provides for the initial recognition of the investment at cost and subsequent value adjustment based on the relevant share of the shareholders’ equity of the subsidiary.

The differences between the value of the equity investment and the shareholders’ equity of the relevant subsidiary are included in the accounting value of the subsidiary.

In the valuation of the relevant share, any potential voting rights are not taken into consideration.

The relevant share of the annual results of the subsidiary is shown in a specific item of the consolidated income statement.

If there is evidence that the value of an equity investment may be impaired, the recoverable value of said equity investment is estimated by considering the present value of future cash flows that the investment could generate, including the final disposal value of the investment. Should the recovery value prove lower than the book value, the difference is recognised in the income statement.

The most recent approved (annual or interim) financial statements are used for the consolidation of the investments in associates. In the cases in which the companies do not apply the IAS/IFRS standards and

therefore, for said companies, it has been verified that the possible application of the IAS/IFRS would not have produced significant effects on the Banca Sistema Group's consolidated financial statements.

Derecognition criteria

Equity investments are derecognised from the financial statements when the contractual rights to cash flows deriving from the investment are lost or when the investment is transferred, with the substantial transfer of all related risks and benefits.

Recognition criteria of income components

In accordance with IAS 18, dividends are recorded when the right of the shareholder to receive payment has been established and, therefore, after the date of resolution of the Shareholders' Meeting of the investee company.

8. Property and equipment

Classification criteria

This item includes assets for permanent use, held to generate income, to be leased, or for administrative purposes, such as land, functional property, property investments, technical installations, furniture and fittings and equipment of any nature and works of art.

They also include costs for improvements to third party assets if they can be separated from the assets in question.

If the above costs do not display functional or usefulness-related autonomy, but future economic benefits are expected from them, they are recorded under "other assets" and are depreciated over the shorter period between that of expected usefulness of the improvements in question and the residual duration of the lease. Depreciation is recognised under Other operating charges/income.

Property, plant and equipment also include payments on account for the purchase and restructuring of assets not yet part of the production process and therefore not yet subject to depreciation. "Functional" property, plant and equipment are represented by assets held for the provision of services or for administrative purposes, while property held for "investment purposes" are those held to collect lease rentals and/or held for capital appreciation.

Recognition criteria

Property and equipment are initially recorded at cost, including all costs directly attributable to installation of the asset. Extraordinary maintenance costs and costs for improvements leading to actual improvement of the asset, or an increase in the future benefits generated by the asset, are attributed to the reference assets, and are depreciated based on their residual useful life.

Measurement and recognition criteria for income components

Following initial recognition, "functional" property, plant and equipment are recorded at cost, less accumulated depreciation, and any write-downs for impairment losses, in line with the "cost model" illustrated in paragraph 30 of IAS 16. More specifically, property, plant and equipment are systematically depreciated each year based on their estimated useful life, using the straight-line basis method apart from:

- land, regardless of whether this was purchased separately or was incorporated into the value of the building, which, insofar as it has an indefinite useful life, is not depreciated;
- works of art, which are not depreciated as their useful life cannot be estimated and their value typically appreciates over time;
- property investments which are recorded at fair value in accordance with IAS 40.

For assets acquired during the financial year, depreciation is calculated on a daily basis from the date of entry into use of the asset. For assets transferred and/or disposed of during the financial year, depreciation is calculated on a daily basis until the date of transfer and/or disposal.

At the end of each year, if there is any evidence that property, plant or equipment that is not held for investment purposes may have suffered an impairment loss, a comparison is made between its book value and its recoverable amount, equal to the higher between the fair value, net of any costs to sell, and the related value in use of the asset, intended as the actual value of future cash flows expected from the asset. Any adjustments are recognised to the income statement under "net value adjustments on property, plant and equipment".

If the reasons that led to recognition of the impairment loss cease to apply, a write-back is recorded that may not exceed the value that the asset would have had, net of depreciation calculated in the absence of previous impairment losses. For property, plant and equipment held “for investment purposes”, which come within the area of application of the IAS 40, the measurement is made at the market value determined using independent surveys and the changes in fair value are recorded in the income statement under the item “net result of the fair value measurement of property, plant and equipment and intangible assets”.

Derecognition criteria

Property, plant and equipment is derecognised from the statement of financial position upon disposal thereof or when the asset is permanently withdrawn from use and no future economic benefit is expected from its disposal.

9. Intangible assets

Classification criteria

This item includes non-monetary assets without physical substance that satisfy the following requirements:

- they can be identified;
- they can be monitored;
- they generate future economic benefits.

In the absence of one of the above characteristics, the expense of acquiring or generating the asset internally is recorded as a cost in the year in which it was incurred.

Intangible assets include software to be used over several years and other identifiable assets generated by legal or contractual rights.

Goodwill is also included under this item, representing the positive difference between the acquisition cost and fair value of the assets and liabilities acquired as part of a business combination. Specifically, an intangible asset is recognised as goodwill when the positive difference between the fair value of equity components acquired and the acquisition cost represents the future capacity of the equity investment to generate profit (goodwill).

If this difference proves negative (badwill), or if the goodwill offers no justification of the capacity to generate future profit from the equity elements acquired, it is recognised directly to the income statement.

Measurement criteria

The value of the intangible assets is systematically amortised from the time of their input into the production process.

With reference to the goodwill, on an annual basis (or at the time of an impairment loss), an assessment test is carried out on the adequacy of its book value. For this purpose, the Unit generating the financial flows to which the goodwill is attributed, is identified. The amount of any impairment is determined by the difference between the goodwill book value and its recovery value, if lower. This recovery value is equal to the higher amount between the fair value of the Unit that generates the financial flows, net of any sale cost, and its value in use. As stated above, any consequent value adjustments are recognised in the income statement.

Derecognition criteria

An intangible asset is derecognised from the statement of financial position at the time of its disposal and if there are no expected future economic benefits.

10. Non-current assets held for sale

At the date of the financial statements, the company did not hold any “Non-current assets held for sale”.

11. Current and deferred taxes

Income taxes for the period, calculated in compliance with prevailing tax regulations, are recorded in the income statement based on the accrual criteria, in accordance with the recognition in the financial statements of the costs and of the revenues that generated them, apart from those referring to the items directly debited or credited to the shareholders’ equity, where the recognition of the tax is made on the shareholders’ equity in order to be consistent. Allocations for income taxes are calculated based on a prudential estimate of the current, prepaid, and deferred tax burden. More specifically, prepaid and deferred taxes are determined on the basis of the temporary differences between the book value of assets and liabilities and their value for taxation purposes.

Deferred tax assets are recorded in the financial statements to the extent that it is probable that they will be recovered on the basis of the Company’s ability to continue to generate

positive taxable income.

Prepaid and deferred taxes are accounted for at equity level with open balances and without offsetting entries, recording the former under "Tax assets" and the latter under "Tax liabilities".

With respect to current taxes, at the level of individual taxes, the prepayments made are offset with the relevant tax charge, indicating the net imbalance under "current tax assets" or the "current tax liabilities" depending on whether it is positive or negative.

12. Provisions for risks and charges

In line with the requirements of IAS 37, provisions for risks and charges cover liabilities, the amount or timing of which is uncertain, related to current obligations (legal or implicit), owing to a past event for which it is likely that financial resources will be used to fulfil the obligation, on condition that an estimate of the amount required to fulfil said obligation can be made at the financial statements balance sheet date. Where the temporary deferral in sustaining the charge is significant, and therefore the extent of the discounting will be significant, provisions are discounted at current market rates.

The provisions are reviewed at the reference date of the annual financial statements and the interim financial statements and adjusted to reflect the current best estimate. These are recorded under their own items in the income statement in accordance with a cost classification approach based on the "nature" of the cost. Provisions related to future charges for employed personnel relating to the bonus system appear under "personnel costs".

The provisions that refer to risks and charges of a fiscal nature are reported as "income taxes", whereas the provisions connected to the risk of potential losses not directly chargeable to specific items in the income statement recorded as "net allocations for risks and charges".

13. Payables and securities issued

Classification criteria

Amounts due to banks and due to customers include the various forms of inter-banking or client funding deposits (current accounts, demand and bonded deposits, loans,

repurchasing agreements, etc.) whereas securities issued include all the liabilities issued (bond loans not classified as "financial liabilities measured at fair value", etc.).

All the financial instruments issued by the Bank are expressed in the financial statements net of any amounts repurchased and include those that have matured as at the balance sheet date but have not yet been reimbursed.

Recognition criteria

These financial liabilities are initially recognised when the deposits are received or when the debt securities are issued. Initial recognition is based on the fair value of the liabilities, increased by the costs/income of the transaction directly attributable to the acquisition of the financial instrument.

Costs/income having the previously mentioned characteristics that will be repaid by the creditor or that can be considered as standard internal administrative costs are excluded.

The initial fair value of a financial liability is usually equivalent to the amount cashed.

Any derivative contracts included in said financial liabilities, which are subject to the assumptions of IAS 32 and 39, are broken down and measured separately.

Measurement criteria

After the initial recognition, the previously mentioned financial liabilities are valued at amortised cost with the effective interest rate method.

Derecognition criteria

The above financial liabilities are derecognised from the statement of financial position at maturity or when they are extinguished. They are derecognised also in the event of repurchase, even temporary, of the previously-issued securities.

Any difference between the book value of the extinguished liability and the amount paid is recorded in the income statement, under "profit (loss) from disposal or repurchase of: financial liabilities". If the Group, subsequent to the repurchase, re-replaces its own securities on the market, said transaction is considered a new issue and the liability is recorded at the new placement price.

14. Financial liabilities held for trading

At the date of the financial statements, the Company did not have any “Held-for-trading financial liabilities”.

15. Financial liabilities at fair value through profit and loss

At the date of the financial statements, the Company did not have any “financial liabilities carried at fair value”.

16. Currency transactions

The currency assets and liabilities include, in addition to those explicitly designated in a currency other than the Euro, those that include financial indexing clauses associated with the Euro exchange rate with a designated currency or a designated bundle of currencies. In accordance with the conversion methods to be used, the assets and liabilities in currencies are subdivided between monetary and non-monetary items.

Recognition criteria

Foreign currency transactions are recorded, at the time of initial recognition, in Euro, applying the spot exchange rates in force on the date of the transaction to the amount in foreign currency.

Measurement criteria

At each reporting date:

- the monetary elements in foreign currencies are converted using the exchange rate in force at the end of the financial year;
- the non-monetary components valued at historical cost in foreign currency are converted at the exchange rate in effect on the date of the transaction;
- the non-monetary components carried at fair value in a foreign currency are converted at the exchange rate in effect on the date the fair value is determined.

The differences in the exchange rates that result from the settlement of monetary elements or the conversion of monetary elements at rates that differ from the initial conversion rates, or the conversion rates on the date of the previous financial statements, are reported in the income statement for the financial year in which they occur in the “Net profit from trading” or if they relate to financial

assets/liabilities for which the fair value option is used in accordance with IAS 39, in the “Net result of the financial assets and liabilities measured at fair value”.

When a profit or a loss relative to a non-monetary component is recorded in shareholders’ equity, the exchange difference relative to said component is also recognised in shareholders’ equity in the year in which it occurs. On the other hand, if the profits or losses of a non-monetary element are reported in the income statement, the difference in the exchange rate is also reported in the income statement in the year in which they occur as stated above.

17. Other information

17.1. Employee termination indemnities

According to the IFRIC, the Employee termination indemnities can be equated with a post-employment-benefit of the “defined-benefit plan type”) which, based on IAS 19, is to be calculated via actuarial methods. Consequentially, the end of the year measurement of the posting in question is made based on the accrued benefits method using the unit credit criteria anticipated (Projected Unit Credit Method).

This method calls for the projection of the future disbursements based on historical, statistical, and probabilistic analysis, as well as in virtue of the adoption of appropriate demographic fundamentals. It allows the severance package accrued at a certain date to be calculated actuarially, distributing the expense for all the years of estimated remaining permanence of the existing workers, and no longer as an expense to be paid if the company ceases its activity on the reporting date.

The actuarial profits and losses, defined as the difference between the book value of the liability and the present value of the obligation at year end, are recognized in shareholders’ equity.

An independent actuary assesses the severance package in compliance with the method indicated above.

17.2. Repurchase agreements

The “repurchase agreements” that oblige the party selling the subject matter of the transaction (for example securities) to repurchase them in the future and the

“securities lending” transactions where the guarantee is represented by cash, are considered equivalent to swap operations and, therefore, the amounts received and disbursed appear in the financial statements as payables and receivables. In particular, the previously mentioned transactions “repurchase agreements” and “securities lending” transactions are recorded in the financial statements as payables for the spot value received, while that for investments are recorded as receivables for the spot price paid. Such transactions do not result in changes in the securities portfolio. Consistently, the cost of funds and the income from the investments, consisting of accrued dividends on the securities and from the difference between the spot price and the forward price thereof, are recorded for the accrual period under the interest items in the income statement.

17.3. Criteria for determining the fair value of financial instruments

Fair value is defined as “the price that would be collected for the sale of an asset or also that would be paid for the transfer of a liability in an orderly transaction between market participants”, at a specific measurement date, excluding forced-type transactions. Underlying the definition of fair value in fact is the presumption that the company is in operation, and that it has no intention or need to liquidate, significantly reduce the volume of its assets, or engage in a transaction at unfavourable terms.

In the case of financial instruments listed in active markets, the fair value is determined based on the deal pricing (official price or other equivalent price on the last stock market trading day of the financial year of reference) of the most advantageous market to which the Group has access. For this purpose, a financial instrument is considered to be listed in an active market if the quoted prices are readily and regularly available from a price list, trader, intermediary, industrial sector, agencies that determine prices, or regulatory authority and said prices represent actual market transactions that regularly take place in normal dealings.

In the absence of an active market, the fair value is determined using measurement techniques generally accepted in financial practice, aimed at establishing what

price the financial instrument would have had, on the valuation date, in a free exchange between knowledgeable and willing parties. Such measurement techniques require, in the hierarchical order in which they are presented, the use:

- of the most recent NAV (Net Asset Value) published by the management investment company for the harmonized funds (UCITS - Undertakings for Collective Investment in Transferable Securities), the Hedge Funds and the SICAVs;
- of the recent transaction prices observable in the markets;
- of the price indications deducible from infoproviders (e.g., Bloomberg, Reuters);
- of the fair value obtained from measurement models (for example, Discounting Cash Flow Analysis, Option Pricing Models) that estimate all the possible factors that influence the fair value of a financial instrument (cost of money, credit exposure, liquidity risk, volatility, foreign exchange rates, prepayment rates, etc.) based on data observable in the market, also with regards to similar instruments on the measurement date. If market data cannot be referenced for one or more risk factors, metrics internally determined on a historical-statistical basis are used. The measurement models are subject to periodic review to guarantee complete and constant reliability;
- of the price indications provided by the counterparty issuer adjusted if necessary to take into account the counterparty and/or liquidity risk (for example, the price resolved on by the Board of Directors and/or the Shareholders’ meeting for the shares of unlisted cooperative bank, the unit value communicated by the management investment company for the closed-end funds reserved to institutional investors or for other types of UCIs other than those cited in paragraph 1, the redemption value calculated in compliance with the issue regulation for the insurance contracts);
- for the equity-linked instruments, where the measurement techniques pursuant to the previous paragraphs are not applicable: i) the value resulting

from independent surveys if available; ii) the value corresponding to the portion of shareholders' equity held resulting from the company's most recent financial statements approved; iii) the cost, adjusted if necessary to take into account significant reductions in value, where the fair value cannot be reliably determined.

Based on the foregoing considerations and in compliance with the IFRS, the Group classifies the measurements at fair value based on a hierarchy of levels that reflects the significance of the inputs used in the measurements.

The following levels are noted:

- **Level 1** - prices (without adjustments) reported on an active market: the measurements of the financial instruments quoted on an active market based on quotations that can be understood from the market;
- **Level 2** - the valuation is not based on prices of the same financial instrument subject to valuation, but on prices or credit spreads obtained from the official prices of essentially similar instruments in terms of risk factors, by using a given calculation method (pricing model).

The use of this approach translates to the search for transactions present on active markets, relating to instruments that, in terms of risk factors, are comparable with the instrument subject to valuation. The calculation methods (pricing models) used in the comparable approach make it possible to reproduce the prices of financial instruments quoted on active markets (model calibration) without including discretionary parameters - i.e. parameters whose value cannot be obtained from the prices of financial instruments present on active markets or cannot be fixed at levels as such to replicate prices present on active markets - which may influence the final valuation price in a decisive manner.

- **Level 3** - inputs that are not based on observable market data: the measurements of financial instruments not quoted on an active market, based on measurement techniques that use significant inputs that are not observable on the market, involving the adoption of estimates and assumptions by management (prices supplied by

the issuing counterparty, taken from independent surveys, prices corresponding to the fraction of the shareholders' equity held in the company or obtained using measurement models that do not use market data to estimate significant factors that condition the fair value of the financial instrument). This level includes measurements of financial instruments at cost price.

17.4 Business combinations

A business combination involves the combination of separate companies or business activities in a single party who has to draft the financial statements. A business combination may give rise to a participatory relation between the parent company (acquirer) and the subsidiary (acquired). A business combination may also provide for the acquisition of the net assets of another entity, including any goodwill, or the acquisition of another entity's capital (mergers and contributions). Based on the provisions of IFRS 3, business combinations must be accounted for by applying the acquisition method, which comprises the following phases:

- identification of the acquirer;
- determination of the cost of the business combination;
- allocation, on the acquisition date, of the business combination cost in terms of the assets acquired and the liabilities, and potential liabilities taken on.

More specifically, the cost of a business combination must be determined as the total fair value as at the date of exchange of the assets transferred, liabilities incurred or assumed, capital instruments issued by the acquirer in exchange for control of the acquired company and all costs directly attributable to the business combination.

The acquisition date is the date on which control of the acquired company is actually obtained. If the acquisition is completed through a single transfer, the date of the transfer will be the acquisition date.

If the business combination is carried out through several transfers:

- the cost of the combination is the overall cost of the individual operations
- the exchange date is the date of each exchange

operation (namely the date on which each investment is recorded in the acquiring company's financial statements), whereas the acquisition date is the one on which control is obtained over the acquired company.

The cost of a business combination is assigned by recording the assets, liabilities and potential liabilities that are identifiable in the acquired company, at the relevant fair values at the date of acquisition.

The assets, liabilities and potential liabilities that can be identified in the acquired company are recorded separately on the acquisition date only if, on this date, they meet the following criteria:

- if an asset is not an intangible asset, it is probable that any future connected economic benefits will flow to the acquiring company and it is possible to assess its fair value reliably;
- if a liability is not a potential liability, it is probable that, in order to extinguish the obligation, investment in resources will be required to produce economic benefits and it is possible to assess the fair value reliably;
- in the case of an intangible asset or a potential liability, the relevant fair value may be assessed reliably.

The positive difference between the cost of the business combination and the acquiring body's profit sharing at the fair value net of the assets, liabilities and potential identifiable liabilities, must be accounted for as goodwill.

After the initial recognition, the goodwill acquired in a business combination is measured at the relevant cost and is submitted to an impairment test at least once a year.

If the difference is negative, a new measurement is made. This negative difference, if confirmed, is recorded immediately as revenue in the income statement.

17.5 Derecognition

This is the removal from the statement of financial position of a financial asset or liability that had previously been recognised.

Before assessing the existence of the conditions for removing financial assets from the financial statements, it has to be checked whether these conditions must

be applied to these assets as a whole or only in part in accordance with IAS 39.

The cancellation rules are applied to the part of the financial assets to be transferred only if at least one of the following requirements have been met:

- the part comprises only cash flows that relate to a financial asset (or a group of assets) that are specifically identified (for example, only the portion of interest relating to the asset);
- the part comprises the cash flows in accordance with a precisely identified percentage of their total (for example, 90% of all cash flows deriving from the asset);
- the part includes a precisely identified portion of specifically identified cash flows (for example, 90% of cash flows only of the portion relating to the asset).

If the aforementioned criteria are not met, the cancellation standards must apply to the financial asset (or group of financial assets) as a whole.

The conditions for the complete cancellation of a financial asset are the extinction of the contractual rights, such as their natural maturity, or the transfer to another counterparty of cash flows deriving from this asset.

Payment rights are considered to be transferred if contractual rights are held to receive the financial flows from the asset, but an obligation is assumed to pay these flows to one or more entities and all three of the following conditions are satisfied (pass-through agreement):

- the Group is under no obligation to pay out amounts uncollected from the original assets;
- the sale and offering as guarantees of the original asset is prohibited, except if it guarantees the obligation to pay financial flows;
- the Group is obliged to transfer immediately all the financial flows that it receives and has no right to invest them, except for investments in liquid assets during the short period between the collection and payment dates, on condition that the interest matured over the period is paid.

In addition, the elimination of a financial asset is subject to a check being carried out that all the risks and benefits deriving from holding the rights have effectively been

transferred (true sale). If there is a transfer of substantially all the risks and benefits, the transferred asset (or group of assets) will be cancelled and the rights and obligations relating to the transfer will be recorded as assets or liabilities.

On the other hand, if the risks and benefits are maintained, the transferred asset (or group of activities) must continue to be recognised. In that case, a liability corresponding to the amount received as consideration for the transfer, and subsequently, all the income accrued on the assets as well as all the expenses accrued on the liabilities must be recorded.

The main operations that do not allow a financial asset to be cancelled fully are the receivable securitisation operations, the repurchase agreements and the security lending transactions based on the aforementioned rules.

In the case of repurchase agreements and security lending transactions, the assets that are the object of the transactions are not removed from the financial statements since the terms of the transactions require all the associated risks and benefits to be maintained.

17.6 Introduction of the “bilateral CVA” to the valuation of derivatives

IFRS 13 - applicable from 1 January 2013 - establishes the need to consider, in the fair value of derivative contracts, the risk of non-performance (risk of one of the two parties in the contract not fulfilling their obligations) both at the time of initial recognition and in subsequent valuations. This risk includes:

- changes in the entity’s creditworthiness, for which, in determining the fair value of derivatives, the risk of non-fulfilment of obligations must also be considered;
- changes in the counterparty creditworthiness.

The fair value of a derivative instrument can be broken down into various components that include the effect of the various underlying risk factors.

1. The collateralised component of the fair value is calculated as if the contract was subject to a perfect collateral agreement, as such to reduce the counterparty’s risk to a negligible level. In practice, said situation can be brought closer with the CSA (Credit Support Annex) which

makes provision for daily margining, zero threshold and minimum transfer amount and overnight flat rate. This component of fair value includes the market risk (e.g. with respect to underlying assets, volatility, etc.) and the risk of financing implicit in the CSA (overnight rate loan, OIS discounting method).

2. The component, known as the Bilateral Credit Value Adjustment (bCVA), takes into consideration the possibility of the counterparties (Counterparty and Investor) going bankrupt and is in turn given by two addends, called the Credit Value Adjustment (CVA) and Debit Value Adjustment (DVA), that represent the following scenarios:

- the CVA (negative) takes into consideration the scenarios in which the Counterparty (Customer) goes bankrupt before the Investor (Bank), and the latter presents a positive exposure to the Counterparty. In these scenarios, the Investor suffers a loss equal to the cost of replacement of said derivative;
- the DVA (positive) takes into consideration the scenarios in which the Investor goes bankrupt before the Counterparty, and the former presents a negative exposure to the Counterparty. In these scenarios, the Investor benefits from a profit equal to the cost of replacement of said derivative.

The calculation of the latter component of fair value is performed by taking into consideration the presence of netting arrangements and collateral agreements allowing the counterparty’s risk to be mitigated. In the first case, the presence of the netting arrangement determines the performance of the calculation of the bilateral CVA on a portfolio including all transactions subject to netting in place with that same Counterparty. Consequently, in the presence of netting arrangements, both the CVA component and the DVA component decrease in absolute terms, in order to mitigate the counterparty risk they cause.

In the case of CSA contracts (collateral) with daily margining, reduced thresholds and Minimum Transfer Amounts, counterparty risk can be considered negligible. Therefore, the calculation of the bCVA only considers the transactions not covered by CSA. By contrast, in the case of a CSA with thresholds and Minimum Transfer

Amounts that are not negligible, the bCVA is calculated based on the materiality approach.

The bCVA calculation depends on the creditworthiness of the Investor and Counterparty, available via recourse to various sources. The Risk Management Department, in collaboration with the Administrative and Fiscal management, defined a rule allowing the creditworthiness data to be selected as a function of its availability. The rule provides as follows:

- in the case of counterparties with a CDS spread quoted on the market, the bCVA is calculated by considering the risk-neutral probability of default (i.e. estimated based on the prices of bonds and not based on historical data) quoted on the market and relating to both the Counterparty and the Investor, measured based on the quoted CDS spread credit curve;
- in the case of Large Corporate counterparties without a CDS quoted on the market with

turnover greater than the critical threshold, the bCVA is calculated by considering the risk-neutral probability of default of a counterparty that is associated to the contract counterparty (comparable approach).

Creditworthiness is measured:

- for Project Finance counterparties using the CDS spread credit curve (Industrial comparable);
- for other counterparties using the CDS spread credit curve (comparable for the counterparty);
- in the case of illiquid counterparties not included in the previous categories, the bCVA is calculated by considering the probability of default of the counterparty and of the Group, determined using the credit curve obtained from the probability of default matrices.

The application of the standard did not have any significant effects on the Group, since its portfolio is almost entirely composed of short-term assets.

A.3 - INFORMATION ON TRANSFERS BETWEEN PORTFOLIOS OF FINANCIAL ASSETS

A.3.1 Reclassified financial assets: book value, fair value and effects on comprehensive income

No financial instruments were transferred between portfolios.

A.3.2 Reclassified financial assets: effects on overall profit before transfer

No financial assets were reclassified.

A.3.3 The transfer of financial assets held for trading

No financial assets held for trading were transferred.

A.3.4 Effective interest rate and expected cash flows from the reclassified assets

No cash flows are expected from the reclassified assets.

A.4 - INFORMATION ON FAIR VALUE

QUALITATIVE INFORMATION

A.4.1 Fair value levels 2 and 3: measurement techniques and inputs used

Please refer to the accounting policies.

A.4.2 Processes and sensitivity of valuations

The book value was assumed as a reasonable approximation of the fair value.

A.4.3 Fair value hierarchy

In order to prepare the financial statements, the fair value hierarchy used was the following:

- Level 1 - Effective market quotes the valuation is the market price of said financial instrument subject to valuation, obtained on the basis of quotes expressed by an active market.
- Level 2 - Comparable Approach
- Level 3 - Mark-to-Model Approach

A.4.4 Other Information

The item is not applicable for the Group.

A.4.5 Fair value hierarchy

A.4.5.1 Assets and liabilities measured at fair value on a recurring basis: breakdown by fair value levels.

Financial assets/liabilities measured at fair value	31/12/2016			31/12/2015		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
1. Financial assets held for trading	996	-	-	-	-	-
2. Financial assets at fair value through profit and loss	-	-	-	-	-	-
3. Financial assets available for sale	509,838	-	5,000	920,402	-	5,000
4. Hedging derivatives	-	-	-	-	-	-
5. Property and equipment	-	-	-	-	-	-
6. Intangible assets	-	-	-	-	-	-
TOTAL	510,834	-	5,000	920,402	-	5,000
1. Held-for-trading financial liabilities	-	-	-	-	-	-
2. Financial liabilities at fair value through profit and loss	-	-	-	-	-	-
3. Hedging derivatives	-	-	-	-	-	-
TOTAL	-	-	-	-	-	-

Key:
L1 = Level 1
L2 = Level 2
L3 = Level 3

On.4.5.2 Annual changes of assets measured at fair value based on a recurring basis (level 3)

	Financial assets held for trading	Financial assets at fair value through profit and loss	Financial assets available for sale	Hedging derivatives	Property and equipment	Intangible assets
1. Opening balance	-	-	5,000	-	-	-
2. Increases	-	-	-	-	-	-
2.1 Purchases	-	-	-	-	-	-
2.2 Profits booked to:	-	-	-	-	-	-
2.2.1 Income Statement	-	-	-	-	-	-
- of which: Capital gains	-	-	-	-	-	-
2.2.2 Shareholders' equity	-	-	-	-	-	-
2.3 Transfers from other levels	-	-	-	-	-	-
2.4 Other increases	-	-	-	-	-	-
3. Decreases	-	-	-	-	-	-
3.1 Sales	-	-	-	-	-	-
3.2 Refunds	-	-	-	-	-	-
3.3 Losses booked to:	-	-	-	-	-	-
3.3.1 Income Statement	-	-	-	-	-	-
- of which Capital loss	-	-	-	-	-	-
3.3.2 Shareholders' equity	-	-	-	-	-	-
3.4 Transfers to other levels	-	-	-	-	-	-
3.5 Other decreases	-	-	-	-	-	-
4. Closing balance	-	-	5,000	-	-	-

A.4.5.4 Assets and liabilities not measured at fair value or measured at fair value on a non-recurring basis:

Breakdown by fair value levels

Assets and liabilities not measured at fair value or measured at fair value on a non-recurring basis	31/12/2016				31/12/2015			
	BV	L1	L2	L3	BV	L1	L2	L3
1. Financial assets held to maturity	-	-	-	-	-	-	-	-
2. Due from banks	83,493	-	-	83,493	2,076	-	-	2,076
3. Loans to customers	1,348,329	-	-	1,348,329	1,457,990	-	-	1,457,990
4. Property and equipment held for investment	-	-	-	-	-	-	-	-
5. Non-current assets and groups of assets held for sale	-	-	-	-	-	-	-	-
Total	1,431,822	-	-	1,431,822	1,460,066	-	-	1,460,066
1. Due to banks	458,126	-	-	458,126	362,075	-	-	362,075
2. Due to customers	1,262,123	-	-	1,262,123	1,878,339	-	-	1,878,339
3. Securities issued	90,330	-	-	90,330	20,102	-	-	20,102
4. Liabilities associated with assets held for sale	-	-	-	-	-	-	-	-
Total	1,810,579	-	-	1,810,579	2,260,516	-	-	2,260,516

Key:
 BV = Book Value
 L1 = Level 1
 L2 = Level 2
 L3 = Level 3

A.5 INFORMATION CONCERNING "DAY ONE PROFIT/LOSS"

Nothing to report.

PART B - INFORMATION ON THE CONSOLIDATED STATEMENT OF FINANCIAL POSITION

ASSETS

SECTION 1 - CASH AND CASH EQUIVALENTS - ITEM 10

1.1 Cash and cash equivalents: breakdown

Items/Values	31/12/2016	31/12/2015
a. Cash	98	104
b. Demand deposits with Central Banks	-	-
TOTAL	98	104

SECTION 2 - HELD-FOR-TRADING FINANCIAL ASSETS - ITEM 20

2.1 Held-for-trading financial assets: breakdown by product

Items/Values	31/12/2016			31/12/2015		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
A. Non-derivative financial assets						
1. Debt securities	-	-	-	-	-	-
1.1 Structured securities	-	-	-	-	-	-
1.2 Other debt securities	-	-	-	-	-	-
2. Equity securities	996	-	-	-	-	-
3. Units of UCI	-	-	-	-	-	-
4. Loans	-	-	-	-	-	-
4.1 Reverse repurchase agreements	-	-	-	-	-	-
4.2 Other	-	-	-	-	-	-
TOTAL A	996	-	-	-	-	-
B. Derivative instruments						
1. Financial derivatives	-	-	-	-	-	-
1.1 for trading	-	-	-	-	-	-
1.2 connected with the fair value option	-	-	-	-	-	-
1.3 other	-	-	-	-	-	-
2. Credit derivatives	-	-	-	-	-	-
2.1 for trading	-	-	-	-	-	-
2.2 connected with the fair value option	-	-	-	-	-	-
2.3 other	-	-	-	-	-	-
TOTAL B	-	-	-	-	-	-
TOTAL (A+B)	996	-	-	-	-	-

2.2 Held-for-trading financial assets: breakdown by debtors/issuers

Items/Values	31/12/2016	31/12/2015
A. Non-derivative financial assets	-	-
1. Debt securities	-	-
a) Governments and Central Banks	-	-
b) Other public institutions	-	-
c) Banks	-	-
d) Other issuers	-	-
2. Equity securities	996	-
a) Banks	-	-
b) Other issuers:	996	-
- insurance companies	-	-
- financial companies	-	-
- non-financial companies	996	-
- other	-	-
3. Units of UCI	-	-
4. Loans	-	-
a) Governments and Central Banks	-	-
b) Other public institutions	-	-
c) Banks	-	-
d) Other subjects	-	-
Total A	996	-
B. Derivative instruments	-	-
a) Banks	-	-
- fair value	-	-
b) Customers	-	-
- fair value	-	-
Total B	-	-
Total (A+B)	996	-

SECTION 4 - AVAILABLE-FOR-SALE FINANCIAL ASSETS - ITEM 40

4.1 Available-for-sale financial assets: breakdown by product

Items/Values	31/12/2016			31/12/2015		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
1. Debt securities	507,873	-	-	920,402	-	-
1.1 Structured securities	-	-	-	-	-	-
1.2 Other debt securities	507,873	-	-	920,402	-	-
2. Equity securities	1,965	-	5,000	-	-	5,000
2.1 Measured at fair value	1,965	-	5,000	-	-	5,000
2.2 Measured at cost	-	-	-	-	-	-
3. Units of UCI	-	-	-	-	-	-
4. Loans	-	-	-	-	-	-
Total	509,838	-	5,000	920,402	-	5,000

The AFS portfolio is predominantly made up of Italian government securities with a short-term maturity.

The equity security refers to the equivalent value of the interest in Bank of Italy.

4.2 Available-for-sale financial assets: breakdown by debtors/issuers

Items/Values	31/12/2016	31/12/2015
1. Debt securities	507,873	920,402
a) Governments and Central Banks	507,873	920,402
b) Other public institutions	-	-
c) Banks	-	-
d) Other issuers	-	-
2. Equity securities	6,965	5,000
a) Banks	5,000	5,000
b) Other issuers	1,965	-
- insurance companies	-	-
- financial companies	-	-
- non-financial companies	1,965	-
- other	-	-
3. Units of UCI	-	-
4. Loans	-	-
a) Governments and Central Banks	-	-
b) Other public institutions	-	-
c) Banks	-	-
d) Other subjects	-	-
TOTAL	514,838	925,402

SECTION 5 - HELD-TO-MATURITY FINANCIAL ASSETS - ITEM 50

The portfolio was not used during the year.

SECTION 6 - DUE FROM BANKS - ITEM 60

6.1 Due from banks: breakdown by product

Type of transactions/Values	31/12/2016				31/12/2015			
	BV	FV			BV	FV		
		Level 1	Level 2	Level 3		Level 1	Level 2	Level 3
A. Due from Central Banks	62,441	-	-	-	1,909	-	-	-
1. Term deposits	-	X	X	X	-	X	X	X
2. Compulsory reserve	62,441	X	X	X	1,909	X	X	X
3. Repurchase agreements	-	X	X	X	-	X	X	X
4. Other	-	X	X	X	-	X	X	X
B. Due from banks	21,051	-	-	-	167	-	-	-
1. Loans	21,051	-	-	-	167	-	-	-
1.1 Current accounts and demand deposits	8,671	X	X	X	167	X	X	X
1.2. Term deposits	12,030	X	X	X	-	X	X	X
1.3. Other loans:	350	-	-	-	-	-	-	-
- Reverse repurchase agreements	-	X	X	X	-	X	X	X
- Financial leases	-	X	X	X	-	X	X	X
- Other	350	X	X	X	-	X	X	X
2. Debt securities	-	-	-	-	-	-	-	-
2.1 Structured securities	-	X	X	X	-	X	X	X
2.2 Other debt securities	-	X	X	X	-	X	X	X
Total	83,492	-	-	83,492	2,076	-	-	2,076

Key:
BV = BOOK VALUE
FV = FAIR VALUE

The item mostly included the liquidity for the legal reserves c/o Bank of Italy; the Bank is a direct participant at the gross Target II regulation.

SECTION 7 - LOANS TO CUSTOMERS - ITEM 70

7.1 Loans to customers: breakdown by product

Type of transactions/ Values	31/12/2016						31/12/2015					
	Book value			Fair Value			Book value			Fair Value		
	Performing	Non-performing		L1	L2	L3	Performing	Non-performing		L1	L2	L3
Purchased		Other	Purchased					Other				
Loans	1,241,026	1,059	106,244	-	-	1,348,329	1,373,774	2,216	82,000	-	-	1,457,990
1. Current accounts	12,249	-	5	X	X	X	13,878	-	28	X	X	X
2. Reverse repurchase agreements	-	-	-	X	X	X	177,868	-	-	X	X	X
3. Mortgage loans	62,857	-	16,119	X	X	X	74,894	-	8,216	X	X	X
4. Credit cards, personal loans and salary- or pension-backed loans	265,829	-	320	X	X	X	119,850	-	938	X	X	X
5. Financial leases	-	-	-	X	X	X	-	-	-	X	X	X
6. Factoring	795,012	1,059	89,744	X	X	X	861,507	2,216	72,795	X	X	X
7. Other loans	105,079	-	56	X	X	X	125,777	-	23	X	X	X
Debt securities	-	-	-				-	-	-			
8. Structured securities	-	-	-	X	X	X	-	-	-	X	X	X
9. Other debt securities	-	-	-	X	X	X	-	-	-	X	X	X
TOTAL (book value)	1,241,026	1,059	106,244	-	-	1,348,329	1,373,774	2,216	82,000	-	-	1,457,990

The item may mostly include the amount of the credit acquired by the Group, in connection with its factoring activities.

The debt exposure of the factoring activities mainly refers to activities within Public Administration, in particular with Local health authorities and Territorial Entities.

7.2 Loans to customers: breakdown by debtors/issuers

Type of transactions/Values	31/12/2016			31/12/2015		
	Performing	Non-performing		Performing	Non-performing	
		Purchased	Other		Purchased	Other
1. Debt securities:	-	-	-	-	-	-
a) Governments	-	-	-	-	-	-
b) Other Public institutions	-	-	-	-	-	-
c) Other issuers	-	-	-	-	-	-
- non-financial companies	-	-	-	-	-	-
- financial companies	-	-	-	-	-	-
- insurance companies	-	-	-	-	-	-
- other	-	-	-	-	-	-
2. Loans to:	1,241,026	1,059	106,244	1,373,774	2,216	82,000
a) Governments	236,261	-	736	273,962	-	1,631
b) Other Public institutions	421,026	1,059	58,924	521,021	2,216	40,655
c) Other parties	583,739	-	46,584	578,791	-	39,714
- non-financial companies	301,203	-	44,975	252,569	-	38,198
- financial companies	15,361	-	-	198,607	-	-
- insurance companies	2	-	1	-	-	-
- other	267,173	-	1,608	127,615	-	1,516
TOTAL	1,241,026	1,059	106,244	1,373,774	2,216	82,000

SECTION 10 - EQUITY INVESTMENTS - ITEM 100

10.1 Equity investments: information on investment relationships

Names	Registered office	Ownership Interest %	% of votes available
A. Wholly-controlled enterprises			
1. S.F. Trust Holdings Ltd	London	100%	100%
2. Beta Stepstone S.p.A.	Milan	100%	100%
3. Largo Augusto Servizi e Sviluppo S.r.l.	Milan	100%	100%
C. Companies under considerable control			
1. CS Union S.p.A.	Cuneo, Italy	10%	10%

10.3 Significant equity investments: accounting information

Names	Cash and cash equivalents	Financial assets	Non-financial assets	Financial liabilities	Non-financial liabilities	Total income	Interest margin	Net value adjustments to property and equipment/intangible assets	Profit (Loss) before tax from continuing operations	Profit (Loss) after tax from continuing operations	Profit (Loss) on groups of assets held for sale after tax	Profit (Loss) for the year	Other income items (after taxes)	Overall profitability
A. Wholly-controlled enterprises														
1. S.F. Trust Holdings Ltd	-	63	682	1,157	151	-	(46)	(6)	(199)	(199)	-	(199)	-	(199)
2. Beta Stepstone S.p.A.	2	83,917	5,316	19,575	7,297	3,051	2,606	(8)	1,638	1,288	-	1,288	-	1,288
3. Largo Augusto Servizi e Sviluppo S.r.l.	-	-	22,636	18,566	200	-	(61)	-	(160)	(130)	-	(130)	-	(130)

10.4 Non-significant equity investments: accounting information

Names	Book value of equity investments	Total assets	Total liabilities	Total income	Profit (Loss) after tax from continuing operations	Profit (Loss) on groups of assets held for sale after tax	Profit (Loss) for the year	Other income items (after taxes)	Overall profitability
C. Companies under considerable control									
1. CS Union SpA	2,378	40,148	36,661	8,440	9,389	-	526	-	526

Figures presented in accordance with the International Accounting Standards.

10.5 Equity investments: annual changes

	31/12/2016	31/12/2015
A. OPENING BALANCE	2,696	2,448
B. INCREASES	31	248
B.1 Purchases	-	-
B.2 Write-backs	-	-
B.3 Revaluations	-	-
B.4 Other changes	31	248
C. DECREASES	1,697	-
C.1 Sales	1,697	-
C.2 Impairment losses	-	-
C.3 Other changes	-	-
D. CLOSING BALANCE	1,030	2,696
E. TOTAL REVALUATIONS	-	-
F. TOTAL IMPAIRMENT LOSSES	-	-

SECTION 12 - PROPERTY, PLANT AND EQUIPMENT - ITEM 120

12.1 Property and equipment: composition of the assets valued at cost

	31/12/2016	31/12/2015
1.1. Property and equipment owned	23,313	1,058
a) land	8,416	-
b) buildings	14,055	-
c) furniture	255	282
d) electronic equipment	587	766
e) other	-	10
1.2. Property and equipment acquired under finance lease	-	-
a) land	-	-
b) buildings	-	-
c) furniture	-	-
d) electronic equipment	-	-
e) other	-	-
TOTAL	23,313	1,058

The property and equipment are recorded in the financial statements in accordance with the general acquisition cost criteria, including the accessory charges and any other expenses incurred to place the assets in conditions useful for the company, in addition to indirect costs for the portion reasonably attributable to assets that refer to the costs incurred, as at the end of 2016.

Percent depreciation:

- office furniture: 12%
- furnishings: 15%
- electronic machinery and miscellaneous equipment: 20%
- assets less than Euro 516: 100%

12.5 Property and equipment for business use: annual changes

Assets/Values	Land	Buildings	Furniture	Electronic equipment	Other	Total
A. Gross opening balances	-	-	959	1,552	193	2,704
A.1 Total net value reductions	-	-	677	786	183	1,646
A.2 Net opening balances	-	-	282	766	10	1,058
B. Increases	8,416	14,055	172	177	-	22,820
B.1 Purchases	8,416	14,055	7	7	-	22,485
B.2 Capitalised improvement expenses	-	-	-	-	-	-
B.3 Write-backs	-	-	-	-	-	-
B.4 Positive changes in fair value allocated to	-	-	-	-	-	-
a) shareholders' equity	-	-	-	-	-	-
b) income statement	-	-	-	-	-	-
B.5 Positive foreign exchange differences	-	-	-	-	-	-
B.6 Transfers of properties held for investment	-	-	-	-	-	-
B.7 Other changes	-	-	-	39	-	39
B.8 Business combination transactions	-	-	165	131	-	296
C. Decreases	-	-	199	356	10	565
C.1 Sales	-	-	-	-	-	-
C.2 Depreciation	-	-	49	215	-	264
C.3 Value adjustments for impairment allocated to	-	-	-	-	-	-
a) shareholders' equity	-	-	-	-	-	-
b) income statement	-	-	-	-	-	-
C.4 Negative changes in fair value allocated to	-	-	-	-	-	-
a) shareholders' equity	-	-	-	-	-	-
b) income statement	-	-	-	-	-	-
C.5 Negative foreign exchange differences	-	-	-	-	-	-
C.6 Transfers to:	-	-	-	-	-	-
a) property and equipment held for investment	-	-	-	-	-	-
b) assets held for sale	-	-	-	-	-	-
C.7 Other changes	-	-	71	20	10	101
C.8 Business combination transactions	-	-	79	121	-	200
D. Net closing balance	8,416	14,055	255	587	-	23,313
D.1 Total net value reductions	-	-	876	1,142	-	2,018
D.2 Gross closing balance	8,416	14,055	1,130	1,729	-	25,330
E. Valuation at cost	8,416	14,055	255	587	-	23,313

SECTION 13 - INTANGIBLE ASSETS - ITEM 130

13.1 Intangible assets: breakdown by type of asset

Assets/Values	31/12/2016		31/12/2015	
	Finite useful life	Indefinite useful life	Finite useful life	Indefinite useful life
A.1 Goodwill	-	1,786	-	1,786
A.2 Other intangible assets	49	-	86	-
A.2.1 Assets measured at cost:	49	-	86	-
a. Internally generated intangible assets	-	-	-	-
b. Other assets	49	-	86	-
A.2.2 Assets measured at fair value:	-	-	-	-
a. Internally generated intangible assets	-	-	-	-
b. Other assets	-	-	-	-
TOTAL	49	1,786	86	1,786

The other intangible assets are recorded at purchase cost including also accessory costs, and are systematically amortised over a period of 5 years. The item mainly refers to software.

The goodwill originates from the consolidation of the former Gruppo SF Trust of Solvi S.r.l. which was subsequently merged into the Parent company.

Subsequent to the merger, the former Solvi's assets were fully integrated in those of the Bank with the purpose of pursuing efficiencies both in terms of expected synergies with the other businesses and in terms of overall operating costs.

Since the activities once performed by Solvi Srl., now are now fully integrated and inseparable from the rest of Banca Sistema's operations, the Bank is not currently able to distinguish the expected cash flows of the merged entity from those of the Bank itself.

Therefore, in this specific case, the goodwill of Euro 1.8 million recorded in the financial statements is an asset that cannot be separated from the rest of the Bank.

In particular, the impairment test pursuant to IAS 36 requires that the recoverable value of goodwill be greater than its book value in the financial statements; in detail, as provided for by paragraph 18 of IAS 36, the recoverable amount has been defined as "the higher of the fair value of an asset or of a cash-generating unit having deducted sales costs and its value in use".

Specifically, the impairment test was conducted referring to the "Value in use" based on the flows indicated in the 2017 Budget, in the Bank's business plan in relation to the 2015-2018 period and to a forecast of expected cash flows for the 2019-2021 period, conservatively assuming an estimated growth rate of 1.2% on an annual basis.

The main parameters used for estimation purposes were as follows:

Risk Free Rate + country risk premium	1.5%
Equity Risk Premium	5.5%
Beta	1.2%
Cost of equity	8.2%
Growth rate "g"	2.0%

The estimated value in use obtained based on the parameters used and the growth assumptions is considerably greater than shareholders' equity as at 31 December 2016. Furthermore, considering that the use value was determined via recourse to estimates and assumptions that may introduce elements of uncertainty, sensitivity analysis - as required by the accounting standards of reference - were performed with the purpose of verifying the variations of the results previously obtained as a function of the basic assumptions and parameters.

In particular, the quantitative exercise was completed

by a stress test of the parameters relative to the Bank's growth rate and the discounting rate of the expected cash flows (quantified in an isolated or simultaneous movement of 50bps), that confirmed the absence of impairment indicators, confirming a value in use once again significantly greater than the book value of goodwill in the financial statements.

Considering all the above, no qualitative trigger events that suggest a need for impairment having been identified, the Department deemed it appropriate not to write-down the book value of goodwill posted in the financial statements as at 31 December 2016.

13.2 Intangible assets: annual changes

	Goodwill	Other intangible assets: generated internally		Other intangible assets: Other		Total
		Def	Indef	Def	Indef	
A. Opening balance	1,786	-	-	3,549	-	5,335
A.1 Total net value reductions	-	-	-	3,463	-	3,463
A.2 Net opening balances	1,786	-	-	86	-	1,872
B. Increases	-	-	-	31	-	-
B.1 Purchases	-	-	-	-	-	-
B.2 Increases in internal intangible assets	-	-	-	-	-	-
B.3 Write-backs	-	-	-	-	-	-
B.4 Positive changes in fair value:	-	-	-	-	-	-
- of shareholders' equity	-	-	-	-	-	-
- income statement	-	-	-	-	-	-
B.5 Positive foreign exchange differences	-	-	-	-	-	-
B.6 Other changes	-	-	-	7	-	-
B.8 Business combination transactions	-	-	-	24	-	-
C. Decreases	-	-	-	68	-	68
C.1 Sales	-	-	-	-	-	-
C.2 Impairment losses	-	-	-	68	-	68
- Amortization	-	-	-	68	-	68
- Write-downs:	-	-	-	-	-	-
+ shareholders' equity	-	-	-	-	-	-
+ income statement	-	-	-	-	-	-
B3 Negative changes in fair value:	-	-	-	-	-	-
- of shareholders' equity	-	-	-	-	-	-
- income statement	-	-	-	-	-	-
C.4 Transfers of held-for-sale non-current assets	-	-	-	-	-	-
C.5 Negative foreign exchange differences	-	-	-	-	-	-
C.6 Other changes	-	-	-	-	-	-
D. Net closing balance	1,786	-	-	49	-	1,804
D.1 Total net value adjustments	-	-	-	3,531	-	3,395
E. Gross closing balance	1,786	-	-	3,580	-	5,199
F. Valuation at cost	1,786	-	-	49	-	1,804

Key - Of definite duration | Indef: Of indefinite duration

The item goodwill refers to the incorporation of the subsidiary Solvi S.r.l. which took place on 1 August 2013.

SECTION 14 - TAX ASSETS AND TAX LIABILITIES - ITEM 140 OF ASSETS AND ITEM 80 OF LIABILITIES

14.1 Deferred tax assets: breakdown

Deferred tax liabilities are composed as follows:

	31/12/2016
a) receivable write-downs	3,459
b) write-downs of late-payment interest receivables	-
c) tax losses	30
d) risk provisions	1,297
e) prepaid taxes related to extraordinary transactions	1,395
f) other	1,313
Total	7,494

14.2 Deferred tax liabilities: breakdown

Deferred tax liabilities are composed as follows:

	31/12/2016
a) uncollected late payment interest income	7,040
c) AFS securities	336
d) Other	87
Total	7,463

14.3 Changes in deferred tax assets through profit and loss

	31/12/2016	31/12/2015
1. Initial amount	3,197	2,434
2. Increases	4,245	1,259
2.1 Deferred tax assets recorded in the year	4,245	1,259
a) relative to previous financial years	-	-
b) due to the changes in accounting policies	-	-
c) write-backs	257	-
d) other	1,118	1,259
e) business combination transactions	2,869	-
2.2 New taxes or tax rate increases	-	-
2.3 Other increases	-	-
3. Decreases	499	496
3.1 Deferred tax assets annulled in the year	499	496
a) reversals	499	496
b) write-downs for uncollectible amounts	-	-
c) changes in accounting policies	-	-
d) other	-	-
3.2 Tax rate reductions	-	-
3.3 Other decreases	-	-
a) transformation in tax receivables pursuant to Law 214/2011	-	-
b) other	-	-
4. Final amount	6,943	3,197

14.3.1 Change in deferred tax assets pursuant to Law 214/2011.

	31/12/2016	31/12/2015
1. Initial amount	2,658	2,261
2. Increases	1,611	450
3. Decreases	285	53
3.1 Reversals	72	33
3.2 Transformations in tax receivables	-	-
a) deriving from losses for the year	-	-
b) deriving from tax losses	-	-
3.3 Other decreases	213	20
4. Final amount	3,984	2,658

14.4 Change in deferred tax liabilities (through profit and loss)

	31/12/2016	31/12/2015
1. Initial amount	598	3
2. Increases	7,254	595
2.1 Deferred taxes recorded in the year	7,254	595
a) relative to previous financial years	-	-
b) due to the changes in accounting policies	-	-
c) other	3,231	595
d) business combination transactions	4,023	-
2.2 New taxes or tax rate increases	-	-
2.3 Other increases	-	-
3. Decreases	725	-
3.1 Deferred taxes annulled in the year	725	-
a) reversals	130	-
b) due to the changes in accounting policies	-	-
c) other	595	-
3.2 Tax rate reductions	-	-
3.3 Other decreases	-	-
4. Final amount	7,127	598

14.5 Change in deferred tax assets (recorded in equity)

	31/12/2016	31/12/2015
1. Initial amount	618	277
2. Increases	37	445
2.1 Deferred tax assets recorded in the year	37	445
a) relative to previous financial years	-	-
b) due to the changes in accounting policies	-	-
c) other	37	445
2.2 New taxes or tax rate increases	-	-
2.3 Other increases	-	-
3. Decreases	104	104
3.1 Deferred tax assets annulled in the year	104	104
a) reversals	104	104
b) write-downs for uncollectible amounts	-	-
c) due to the changes in accounting policies	-	-
d) other	-	-
3.2 Tax rate reductions	-	-
3.3 Other decreases	-	-
4. Final amount	551	618

14.6 Change in deferred tax liabilities (recorded in equity)

	31/12/2016	31/12/2015
1. Initial amount	206	3
2. Increases	336	595
2.1 Deferred taxes recorded in the year	336	595
a) relative to previous financial years	-	-
b) due to the changes in accounting policies	-	-
c) other	336	595
2.2 New taxes or tax rate increases	-	-
2.3 Other increases	-	-
3. Decreases	206	-
3.1 Deferred taxes annulled in the year	206	-
a) reversals	-	-
b) due to the changes in accounting policies	-	-
c) other	206	-
3.2 Tax rate reductions	-	-
3.3 Other decreases	-	-
4. Final amount	336	598

SECTION 16 - OTHER ASSETS - ITEM 160

16.1 Other assets: breakdown

	31/12/2016	31/12/2015
Tax advances	10.038	10.179
Work in progress	1.611	1.038
Prepayments not related to a specific item	548	266
Trade receivables	507	-
Leasehold improvements	264	572
Other	1.868	479
Security deposits	68	54
Tax assets	-	-
Total	14.904	12.588

The item is mainly composed of tax advances relative to virtual stamp and withholding taxes on interest expense and to the withholding taxes by Capital Gains. The “work in progress items” predominantly relate to bank transfers allocated to their own items and set to zero in January 2017.

LIABILITIES

SECTION 1 - DUE TO BANKS - ITEM 10

1.1 Due to banks: breakdown by product

Type of transactions/Values	31/12/2016	31/12/2015
1. Due to Central banks	192,850	80,002
2. Due to banks	265,276	282,073
2.1 Current accounts and demand deposits	20,039	10,328
2.2 Term deposits	245,237	271,745
2.3 Loans	-	-
2.3.1 Repurchase agreements	-	-
2.3.2 Other	-	-
2.4 Debts for commitments to repurchase own equity instruments	-	-
2.5 Other payables	-	-
TOTAL	458,126	362,075
Fair value - level 1	-	-
Fair value - level 2	-	-
Fair value - level 3	458,126	362,075
Fair value	458,126	362,075

The item increased compared to 31 December 2015 due to an increase in funding from the ECB.

In June 2016, Banca Sistema participated in the second plan of targeted long-term refinancing operations

("TLTRO-II") for a maximum available amount of €123 million. Total funding from the ECB of €192.8 million was obtained against trade receivables and government bonds.

SECTION 2 - DUE TO CUSTOMERS - ITEM 20

2.1 Due to customers: breakdown by product

Type of transactions/Values	31/12/2016	31/12/2015
1. Current accounts and demand deposits	436,934	335,541
2. Term deposits	443,396	572,357
3. Loans	362,163	939,583
3.1 Repurchase agreements	295,581	909,089
3.2 Other	66,582	30,494
4. Debts for commitments to repurchase own equity instruments	-	-
5. Other amounts due	19,630	30,858
TOTAL	1,262,123	1,878,339
Fair value - level 1	-	-
Fair value - level 2	-	-
Fair value - level 3	1,262,123	1,878,339
Fair value	1,262,123	1,878,339

The item other payables includes collections of €35.6 million from Cassa Depositi e Prestiti, against a guarantee comprising solely loans to SMEs by the Bank.

This also includes payables for receivables acquired but not funded and a payable to assigning companies for factoring operations.

SECTION 3 - SECURITIES ISSUED - ITEM 30

3.1 Securities issued: breakdown by product

Type of securities/ Values	31/12/2016			31/12/2015				
	Book value	Fair Value		Book value	Fair Value			
		Level 1	Level 2	Level 3		Level 1	Level 2	Level 3
A. Securities								
1. Bonds	90,330	-	-	90,330	20,102	-	-	20,102
1.1 structured	-	-	-	-	-	-	-	-
1.2 other	90,330	-	-	90,330	20,102	-	-	20,102
2. Other securities	-	-	-	-	-	-	-	-
2.1 structured	-	-	-	-	-	-	-	-
2.2 other	-	-	-	-	-	-	-	-
TOTAL	90,330	-	-	90,330	20,102	-	-	20,102

3.2 Breakdown of item 30 “Securities issued”: subordinated securities

	Issuer	Type of issue	Coupon	Maturity date	Nominal value	IAS value
Tier 1 capital	Banca Sistema S.p.A.	Innovative equity instruments: mixed rate ISIN IT0004881444	Until 13 June 2023, fixed rate at 7%	Perpetual	8,000	8,018
			From 14 June 2023 floating rate 6-month Euribor + 5.5%			
Tier 2 capital	Banca Sistema S.p.A.	Subordinate ordinary loans (Lower Tier 2): ISIN IT0004869712	6-month Euribor + 5.5%	15/11/2022	12,000	12,085
Total					20,000	20,103

SECTION 8 - TAX LIABILITIES - ITEM 80

The breakdown as well as the change in the deferred tax liabilities were illustrated in Part B Section 14 of assets in these notes to the financial statements.

SECTION 10 - OTHER LIABILITIES - ITEM 100

10.1 Other liabilities: breakdown

	31/12/2016	31/12/2015
Work in progress	27,055	32,785
Tax payables to the Tax Authority and other tax authorities	9,212	12,007
Payments received in the reconciliation phase	8,510	1,823
Accrued expenses	6,439	4,298
Trade payables	6,187	2,260
Due to employees	1,728	1,423
Pension repayments	508	562
Other	188	159
TOTAL	59,827	55,317

SECTION 11 - EMPLOYEE TERMINATION INDEMNITIES - ITEM 110

The actuarial value of the fund was calculated by an external actuary, who issued his appraisal.

11.1 Employee termination indemnities: annual changes

	31/12/2016	31/12/2015
A. OPENING BALANCE	1,303	1,173
B. INCREASES	1,090	562
B.1 Allowances of the year	544	524
B.2 Other changes	132	38
B.3 Business combination transactions	414	
C. DECREASES	395	432
C.1 Benefits paid	372	347
C.2 Other changes	23	85
D. CLOSING BALANCE	1,998	1,303
TOTAL	1,998	1,303

The other decreases mainly refer to employee termination indemnities paid in 2016.

The technical valuations were conducted on the basis of the assumptions described in the following table:

Annual discount rate	1.31%
Annual inflation rate	1.50% for 2016
	1.80% for 2017
	1.70% for 2018
	1.60% for 2019
	2.00% from 2020 onwards
Annual termination indemnities rate increase	2.625% for 2016
	2.850% for 2017
	2.775% for 2018
	2.700% for 2019
	3.000% from 2020 onwards
Annual real salary increase rate	1.00%

The discount rate used for determining the present value of the obligation was calculated, pursuant to paragraph 83 of IAS 19, from the Iboxx Corporate AA index with 10+

duration during the valuation month. To this end, a choice was made to select the yield with a duration comparable to the duration of the set of workers subject to valuation.

SECTION 12 - PROVISIONS FOR RISKS AND CHARGES - ITEM 120

12.1 Provision for risks and charges: breakdown

Items/Values	31/12/2016	31/12/2015
1. Post-employment benefit		
2. Other provisions for risks and charges	4,105	372
2.1 legal disputes	500	-
2.2 personnel charges	279	302
2.3 other	3,326	70
TOTAL	4,105	349

The provision for risks and charges of €4.1 million includes the amount of €3.3 million, representing the estimated future liabilities attributable to Beta, calculated based on

the provisional price allocation in accordance with IFRS 3. The remainder refers to the portion of the 2015 bonus deferred to the following three years.

12.2 Provision for risks and charges: annual changes

	Post-employment benefit	Other provisions	Total
A. Opening balance	-	372	372
B. Increases	-	3,803	3,803
B.1 Allowances of the year	-	3,803	3,803
B.2 Time value changes	-	-	-
B.3 Changes due to discount rate changes	-	-	-
B.4 Other changes	-	-	-
C. Decreases	-	70	70
C.1 Uses in the year	-	-	-
C.2 Changes due to discount rate changes	-	-	-
C.3 Other changes	-	70	70
D. Closing balance	-	4,105	4,105

SECTION 15 - SHAREHOLDERS' EQUITY - ITEMS 140, 160, 170, 180, 190, 200 AND 220

15.1 "Share capital" and "Treasury shares": breakdown

The share capital of Banca Sistema is composed by 80,421,052 ordinary shares with a par value of Euro 0.12 for total paid-in share capital of € 9,651 thousand. All outstanding shares have regular dividend entitlement from 1 January. Based on evidence from the Shareholders'

Register and more recent information available, as at 2 July 2015 the shareholders with stakes of more than 5%, the threshold above which Italian law (art. 120 of the Consolidated Law on Finance) requires disclosure to the investee company and Consob, were as follows:

SHAREHOLDERS	% HELD
SGBS S.r.l. (Management Company)	23.1%
Garbifin	0.5%
Fondazione Sicilia	7.4%
Fondazione Cassa di Risparmio di Alessandria	7.4%
Fondazione Pisa	7.4%
Schroders	6.7%
Market	47.5%

The breakdown of the Group's net equity is shown below:

Items/Values	AMOUNT 2016	AMOUNT 2015
1. Share capital	9,651	9,651
2. Share premium reserve	39,352	39,436
3. Reserves	39,608	26,314
4. (Treasury shares)	(53)	-
5. Valuation reserves	425	350
6. Minority interests	20	-
7. Profit (loss) for the year	25,313	17,607
TOTAL	114,316	93,358

For changes in reserves, please refer to the statement of changes in equity.

15.2 Share capital - Parent Company's number of shares: annual changes

Items/Types	Ordinary	Other
A. Initial number of shares	80,421,052	-
fully paid-up	80,421,052	-
not fully paid-up	-	-
A.1 Treasury shares (-)	-	-
A.2 Outstanding shares: opening balance	80,421,052	-
B. Increases	-	-
B.1 New issues	-	-
on payment:	-	-
- business combination transactions	-	-
- conversion of bonds	-	-
- exercising warrants	-	-
- other	-	-
without consideration:	-	-
- in favour of employees	-	-
- in favour of directors	-	-
- other	-	-
B.2 Disposal of treasury shares	-	-
B.3 Other changes	-	-
C. Decreases	-	-
C.1 Cancellation	-	-
C.2 Purchase of treasury shares	-	-
C.3 Company disposal transactions	-	-
C.4 Other changes	-	-
D. Outstanding shares: closing balance	80,421,052	-
D.1 Treasury shares (+)	-	-
D.2 Existing shares at the end of the year	80,421,052	-
fully paid-up	80,421,052	-
not fully paid-up	-	-

15.4 Reserves earnings: other information

In compliance with art. 2427(7 bis) of the Italian Civil Code, below is the detail of the shareholders' equity item revealing the origin and possibility of use and distributability.

Nature	Value as at 31/12/2016	Possibility of use	Quota available
A) Share capital	9,651	-	-
B) Capital reserves			
Share-premium reserve	39,352	A,B,C	-
Reserve for loss recorded		-	-
C) Reserves earnings:			
Legal reserves	5,542	B	-
Valuation reserve	425	-	-
Extraordinary reserve		A,B,C	-
Profit from previous year	32,898	A,B,C	-
Paid for future capital increase	1,477	-	-
D) Other reserves	(362)	-	-
Total	88,983	-	-
Net profit	25,313	-	-
Total equity	114,296	-	-
Non-distributable quota	-	-	-
Distributable quota	-	-	-

Key:
A: for share capital increase
B: to hedge losses
C: for distribution to shareholders

SECTION 16 - MINORITY INTERESTS - ITEM 210

COMPANY NAMES	31/12/2016
Other investments	20
Total	20

This is the equity of the two special-purpose vehicles, Quinto Sistema S.r.l. and Atlantis S.r.l., whose issued notes have been entirely subscribed by Banca Sistema.

OTHER INFORMATION

1. Guarantees issued and commitments

Transactions	31/12/2016	31/12/2015
1) Financial guarantees issued	45	671
a) Banks	-	-
b) Customers	45	671
2) Commercial guarantees issued	-	45
a) Banks	-	45
b) Customers	-	-
3) Irrevocable commitments to disburse funds	-	-
a) Banks	-	-
I) for specified use	-	-
II) for unspecified use	-	-
b) Customers	-	-
I) for specified use	-	-
II) for unspecified use	-	-
4) Commitments underlying credit derivatives: protection sales	-	-
5) Assets pledged for third-party commitments	-	-
6) Other commitments	-	-
TOTAL	45	716

2. Assets pledged as collateral of liabilities and commitments

Portfolios	31/12/2016	31/12/2015
1. Financial assets held for trading	-	-
2. Financial assets at fair value through profit and loss	-	-
3. Financial assets available for sale	402,657	771,332
4. Financial assets held to maturity	-	-
5. Due from banks	-	-
6. Loans to customers	314,931	107,242
7. Property and equipment	-	-

5. Management and dealing on behalf of third parties

Type of services	AMOUNT
1. Execution of orders on behalf of customers	-
a) Purchases	-
1. regulated	-
2. non-regulated	-
b) Sales	-
1. regulated	-
2. non-regulated	-
2. Portfolio management	-
a) individual	-
b) collective	-
3. Securities custody and administration	1,158,667
a) third-party securities under custody: related to the performance of depository bank services (excluding asset management)	-
1. securities issued by the bank drafting the financial statements	-
2. other securities	-
b) third-party securities under custody (excluding asset management): other	37,343
1. securities issued by the bank drafting the financial statements	3,846
2. other securities	33,497
c) third-party securities deposited with third parties	37,343
d) property deeds deposited with third parties	1,121,324
4. Other transactions	-

PART C - INFORMATION ON THE CONSOLIDATED INCOME STATEMENT

SECTION 1 - INTEREST - ITEMS 10 AND 20

1.1. Interest and similar income: breakdown

Items/Technical forms	Debt securities	Loans	Other transactions	31/12/2016	31/12/2015
1. Financial assets held for trading	-	-	-	-	-
2. Financial assets available for sale	(242)	-	-	(242)	813
3. Financial assets held to maturity	-	-	-	-	-
4. Due from banks	-	40	-	40	8
5. Loans to customers	-	86,523	-	86,523	78,198
6. Financial assets at fair value through profit and loss	-	-	-	-	-
7. Hedging derivatives	-	-	-	-	-
8. Other assets	-	-	-	-	-
TOTAL	(242)	86,563	-	86,321	79,019

1.4 Interest expense and similar expense: breakdown

Items/Technical forms	Payables	Securities	Other transactions	31/12/2016	31/12/2015
1. Due to Central banks	7	-	-	7	84
2. Due to banks	1,789	-	-	1,789	1,115
3. Due to customers	11,384	-	-	11,384	18,586
4. Securities issued	-	2,141	-	2,141	1,228
5. Financial liabilities held for trading	-	-	-	-	-
6. Financial liabilities at fair value through profit and loss	-	-	-	-	-
7. Other liabilities and provisions	-	-	-	-	-
8. Hedging derivatives	-	-	-	-	-
TOTAL	13,180	2,141	-	15,321	21,013

SECTION 2 - NET FEE AND COMMISSION INCOME - ITEMS 40 AND 50

2.1 Fee and commission income: breakdown

Type of services/Values	31/12/2016	31/12/2015
a) guarantees given	1	3
b) credit derivatives	-	-
c) management, dealing and consultancy services:	173	332
1. trading in financial instruments	27	-
2. currency trading	-	-
3. portfolio management	-	-
3.1. individual	-	-
3.2. collective	-	-
4. custody and administration of securities	1	2
5. depositary bank	-	-
6. placement of securities	58	25
7. income from reception and transmission of orders	48	46
8. consultancy services	-	-
8.1. on investments	-	-
8.2. on financial structure	-	-
9. distribution of third party services	39	259
9.1. portfolio management	-	-
9.1.1. individual	-	-
9.1.2. collective	-	-
9.2. insurance products	39	259
9.3. other products	-	-
d) collection and payment services	90	54
e) servicing related to securitisations	-	-
f) services related to factoring	9,139	10,905
g) tax collection services	-	-
h) management of multilateral trading facilities	-	-
i) management of current accounts	69	77
j) other services	1,423	1,371
TOTAL	10,895	12,742

2.2 Fee and commission expense: breakdown

Services/Values	31/12/2016	31/12/2015
a) guarantees received	87	62
b) credit derivatives	-	63
c) management, dealing and consultancy services:	633	359
1. trading in financial instruments	70	108
2. currency trading	-	-
3. portfolio management	-	-
3.1 own portfolio	-	-
3.2 third party portfolios	-	-
4. custody and administration of securities	8	-
5. placement of financial instruments	-	-
6. 'out-of-branch' sale of financial instruments, products and services	555	251
d) collection and payment services	137	141
e) other services	978	949
TOTAL	1,835	1,574

SECTION 3 - DIVIDENDS AND SIMILAR INCOME - ITEM 70

3.1 Dividend and similar income: breakdown

Items/Income	31/12/2016		31/12/2015	
	dividends	income from units of UCI	dividends	income from units of UCI
A. Financial assets held for trading	-	-	-	-
B. Financial assets available for sale	227	-	-	-
C. Financial assets at fair value through profit and loss	-	-	-	-
D. Equity investments	-	-	-	-
Total	227	-	-	-

SECTION 4 - PROFIT (LOSS) ON TRADING - ITEM 80

4.1 Profit (losses) on trading: breakdown

Operations/Income items	Capital gains (A)	Profits from trading (B)	Capital loss (C)	Losses from trading (D)	Net income (loss) [(A+B) - (C+D)]
1. Held for trading financial assets	-	5	(109)	-	(104)
1.1 Debt securities	-	-	-	-	-
1.2 Equities	-	5	(109)	-	(104)
1.3 Units of UCI	-	-	-	-	-
1.4 Loans	-	-	-	-	-
1.5 Other	-	-	-	-	-
2. Financial liabilities held for trading	-	-	-	-	-
2.1 Debt securities	-	-	-	-	-
2.2 Payables	-	-	-	-	-
2.3 Other	-	-	-	-	-
3. Other financial assets and liabilities: foreign ex-change differences	-	-	-	20	20
4. Derivative instruments	-	-	-	-	-
4.1 Financial derivatives:	-	-	-	-	-
On debt securities and interest rates	-	-	-	-	-
On securities and stock indices	-	-	-	-	-
On currencies and gold	-	-	-	-	-
Other	-	-	-	-	-
4.2 Credit derivatives	-	-	-	-	-
TOTAL	-	5	(109)	20	(84)

SECTION 6 - PROFIT (LOSS) FROM DISPOSAL/REPURCHASE - ITEM 100
6.1 Profit (loss) from disposal/repurchase: breakdown

Items/Income components	31/12/2016			31/12/2015		
	Profits	Losses	Net income (loss)	Profits	Losses	Net income (loss)
Financial assets						
1. Due from banks	-	-	-	-	-	-
2. Loans to customers	-	-	-	-	-	-
3. Financial assets available for sale	1,476	(196)	1,280	2,655	(137)	2,518
3.1 Debt securities	1,279	(196)	1,083	2,655	(137)	2,518
3.2 Equities	197	-	197	-	-	-
3.3 Units of UCI	-	-	-	-	-	-
3.4 Loans	-	-	-	-	-	-
4. Financial assets held to maturity	-	-	-	-	-	-
TOTAL ASSETS	1,476	(196)	1,280	2,655	(137)	2,518
Financial liabilities						
1. Due to banks	-	-	-	-	-	-
2. Due to customers	-	-	-	-	-	-
3. Securities issued	-	-	-	-	-	-
TOTAL LIABILITIES	-	-	-	-	-	-

SECTION 8 - NET VALUE ADJUSTMENTS/WRITE-BACKS DUE TO IMPAIRMENT - ITEM 130
8.1 Net value adjustments due to loan impairment: breakdown

Items/Income components	Impairment losses (1)			Write-backs (2)				31/12/2016	31/12/2015
	Individual		Collective	Individual		Collective			
	Write-offs	Other		A	B	A	B		
A. Due from banks:	-	-	-	-	-	-	-	-	
loans	-	-	-	-	-	-	-	-	
debt securities	-	-	-	-	-	-	-	-	
B. Loans to customers:	16	9,161	674	-	-	(86)	-	9,765	(5,439)
Non-performing loans purchased	-	-	-	-	-	-	-	-	-
loans	-	-	-	-	-	-	-	-	-
debt securities	-	-	-	-	-	-	-	-	-
Other receivables	16	9,161	674	-	-	(86)	-	9,765	(5,439)
loans	16	9,161	674	-	-	(86)	-	9,765	(5,439)
debt securities	-	-	-	-	-	-	-	-	-
C. Total	16	9,161	674	-	-	(86)	-	9,765	(5,439)

Key:
A = from interest
B = other write-backs

SECTION 11 - ADMINISTRATIVE EXPENSES - ITEM 180

11.1 Personnel expense: breakdown

Type of expenditure/Values	31/12/2016	31/12/2015
1) Employees	14,093	16,921
a) wages and salaries	9,071	8,232
b) social security charges	2,301	1,843
c) termination indemnities	-	-
d) supplementary benefits	-	-
e) allowance to the provision for employee termination indemnities	525	354
f) allowance to the provision post-employment benefit and similar obligations:	-	-
- defined contribution plans	-	-
- defined benefit plans	-	-
g) payments to external pension funds:	249	217
- defined contribution plans	249	217
- defined benefit plans	-	-
h) costs from share-based payments	-	-
i) other benefits in favour of employees	1,947	6,275
2) Other personnel	14	45
3) Directors and statutory auditors	1,056	532
4) Early retirement costs	-	-
5) Recovery of expenses for employees of the Bank seconded to other entities	-	-
6) Reimbursement of expenses for employees of other entities seconded to the Bank	6	30
TOTAL	15,169	17,528

Other benefits in favour of employees include a gross variable component recognised to the management and linked to the Bank's listing.

11.2 Average number of employees by category

Personnel:

- Senior managers 15
- Managers 31
- Remaining employees 82

11.5 Other administrative expenses: breakdown

Type of expenditure / Values	31/12/2016	31/12/2015
Servicing and collection activities	4,445	6,958
Resolution Fund	1,967	2,469
Consultancy	5,051	4,020
Computer expenses	3,736	3,102
Rent and related fees	1,969	1,753
Indirect taxes and duties	1,519	1,611
Advertising	204	791
Auditing fees	309	874
Other	511	542
Car hire and related fees	716	619
Expense reimbursement and entertainment	691	518
Membership fees	257	250
Infoprovider expenses	431	323
Special purpose vehicle expenses	169	-
Maintenance of movables and real properties	52	109
Telephone and postage expenses	182	184
Stationery and printing	110	151
Insurance	207	67
Discretionary payments	3	9
TOTAL	22,529	24,350

SECTION 12 - NET ALLOWANCE FOR RISKS AND CHARGES - ITEM 190

12.1 Net allowance for risks and charges: breakdown

Member	2016	2015
Allowance for risks and charges - other provisions and risks	-	-
Releasing allowance for risks and charges - other risks and charges	(431)	300
TOTAL	(431)	300

SECTION 13 - NET ADJUSTMENTS TO/RECOVERIES ON PROPERTY AND EQUIPMENT - ITEM 200

13.1 Net value adjustments to property and equipment: breakdown

Asset/Income item	Amortization (a)	Value adjustments for impairment (b)	Write-backs (c)	Net result (a + b - c)
A. Property and equipment				
A.1 Owned	(250)	-	-	(250)
▪ Used in operations	(250)	-	-	(250)
▪ For investment	-	-	-	-
A.2 Acquired in financial lease	-	-	-	-
▪ Used in operations	-	-	-	-
▪ For investment	-	-	-	-
TOTAL	(250)	-	-	(250)

SECTION 14 - NET ADJUSTMENTS TO/WRITE-BACKS ON INTANGIBLE ASSETS - ITEM 210

14.1 Net adjustments to intangible assets: breakdown

Asset/Income item	Amortization (a)	Value adjustments for impairment (b)	Write-backs (c)	Net income (a + b - c)
A. Intangible assets				
A.1 Owned	(58)	-	-	(58)
▪ Generated internally by the company	(58)	-	-	(58)
▪ Other	-	-	-	-
A.2 Acquired in financial lease	-	-	-	-
TOTAL	(58)	-	-	(58)

SECTION 15 - OTHER OPERATING EXPENSES AND INCOME - ITEM 220

15.1 Other operating expenses: breakdown

	2016	2015
Amortization on leasehold improvements	248	257
Other operating expenses	602	241
TOTAL	850	498

15.2 Other operating income: breakdown

	2016	2015
Recoveries of expenses on current accounts and deposits for sundry taxes	271	372
Recoveries of factoring legal expenses	280	-
Recoveries of sundry expenses	24	170
Other Income	425	27
TOTAL	1,000	569

SECTION 16 - PROFIT (LOSS) FROM INVESTMENTS - ITEM 240

16.1 Profit (loss) from investments: breakdown

Income item/Sector	2016	2015
1) Joint venture companies		
A. Income	-	-
1. Revaluations	-	-
2. Profits from disposals	-	-
3. Write-backs	-	-
4. Other Income	-	-
B. Expenses		
1. Write-downs	-	-
2. Value adjustments from impairment	-	-
3. Profits from disposals	-	-
4. Other expenses	-	-
Net income (loss)		-
2) Companies under considerable control		
A. Income	2,281	422
1. Revaluations	-	-
2. Profits from disposals	2,281	-
3. Write-backs	-	-
4. Other income	-	422
B. Expenses	-	-
1. Write-downs	-	-
2. Value adjustments from impairment	-	-
3. Profits from disposals	-	-
4. Other expenses	-	-
Net income (loss)	2,281	422
TOTAL	2,281	422

SECTION 19 - PROFIT (LOSS) FROM DISPOSAL OF INVESTMENTS - ITEM 270

19.1 Profit (loss) from disposal of investments: breakdown

Income item/Values	2016	2015
A. Properties	-	-
- Profits from disposals	-	-
- Losses from disposals	-	-
B. Other assets	-	534
- Profits from disposals	-	534
- Losses from disposals	-	-
NET INCOME	-	534

SECTION 20 - TAXES ON INCOME FROM CONTINUING OPERATIONS - ITEM 290

20.1 Taxes on income from continuing operations: breakdown

Item/Values	2016	2015
1 Current taxes (-)	(8,124)	(8,122)
2 Changes in current taxes of previous years (+/-)	95	49
3 Reduction in current taxes of the year (+)	-	-
3.bis Reduction in current taxes of the year for tax credits pursuant to Law no. 214/2011 (+)	-	-
4 Changes in deferred tax assets (+/-)	586	763
5 Changes in deferred tax liabilities (+/-)	(2,636)	(595)
6 Income tax for the year (-) (-1+/-2+3+/-4+/-5)	(10,079)	(7,905)

SECTION 23 - OTHER INFORMATION

Nothing to report.

SECTION 24 - EARNINGS PER SHARE

Earnings per share (EPS)	2016
Attributable net income (thousands of Euro)	24,481
Average number of outstanding shares (1)	80,408,552
Basic earnings per share (in Euro)	0.304

(1) The average number of shares is calculated net of treasury shares held.

PART D - OTHER COMPREHENSIVE INCOME (CONSOLIDATED)

Analytical statement of other comprehensive income (consolidated)

Items	Gross amount	Income Tax	Net amount
10. Profit (loss) for the year			25,313
Other income items without reversal to the income statement			
20. Property and equipment	-	-	-
30. Intangible assets	-	-	-
40. Defined benefit plans	-	-	(56)
50. Non-current assets held for sale	-	-	-
60. Share of valuation reserves connected with investments carried at equity:	-	-	-
Other income items with reversal to the income statement	-		
70. Hedges of foreign investments:	-		
a) changes in fair value	-	-	-
b) reversal to the income statement	-	-	-
c) other changes	-	-	-
80. Foreign exchange differences:	-		
a) changes in value	-	-	-
b) reversal to the income statement	-	-	-
c) other changes	-	-	-
90. Cash flow hedges:	-		
a) changes in fair value	-	-	-
b) reversal to the income statement	-	-	-
c) other changes	-	-	-
100. Financial assets available for sale	393	130	263
a) changes in fair value	1,015	336	679
b) reversal to the income statement	-	-	-
- adjustments for impairment losses	(623)	(206)	(417)
- profit/loss on sale	-	-	-
c) other changes	-	-	-
110. Non-current assets held for sale:	-	-	
a) changes in fair value	-	-	-
b) reversal to the income statement	-	-	-
c) other changes	-	-	-
120. Share of valuation reserves connected with investments carried at equity:	-	-	-
a) changes in fair value	-	-	-
b) reversal to the income statement	-	-	-
- adjustments for impairment losses	-	-	-
- profit/loss on sale	-	-	-
c) other changes	-	-	-
130. Total other income items	393	130	207
140. Comprehensive income (10+130)	393	130	25,520

SECTION 1 - RISKS OF THE BANKING GROUP

1.1 Credit risk

QUALITATIVE INFORMATION

In order to manage the significant risks to which it is or could be exposed, Banca Sistema has set up a risk management system that reflects the characteristics, size and complexity of its operations.

In particular, this system hinges on four core principles:

- suitable supervision by relevant company bodies and functions;
- satisfactory risk management policies and procedures;
- suitable methods and instruments to identify monitor and manage risks, with suitable measuring techniques; thorough internal controls and independent reviews.

In order to reinforce its ability to manage corporate risks, the Bank established the Risk Management Committee and ALM - extra-board committee, which supports the CEO in defining strategies, risk policies and profitability targets.

The Risk Management Committee continuously monitors the relevant risks and any new or potential risks arising from changes in the working environment or forward-looking operations.

With reference to the new regulation in matters of the operation of the internal control system, in accordance with the principle of collaboration between the control functions, the Internal Control and Risk Management Committee (a committee within a committee) was assigned the role of coordinating all the control functions. The methods used to measure, assess and aggregate risks are approved by the Board of Directors, based on proposals from the Risk department, subject to approval by the Risk Management Committee. In order to measure 'Pillar 1 risks', the Bank has adopted standard methods to calculate the capital requirements for Prudential

Regulatory purposes.

In order to evaluate non-measurable 'Pillar 2 risks', the Bank adopts - where possible - the methods stipulated under Supervisory regulations or those established by trade associations. If there are no such indications, standard market practices by operators working at a level of complexity and with operations comparable to those of the Bank are assessed.

With reference to the new provisions in matters of regulatory supervision (15th update of circular 263 - New regulations for the prudential supervision of banks), a series of obligations on management and risk control, including the Risk Appetite Framework (RAF) and the regulatory instructions defined by the Basel Committee were introduced. The Bank has tied the strategic objectives to the RAF. The key ratios and the respective levels were assessed and the any revisions needed were made while defining the company's annual objectives.

In particular, the RAF was designed with key objectives to verify that over time, the business grows and develops observing capital strength and liquidity obligations, implementing monitoring and alert mechanisms and related series of actions that allow prompt intervention in case of significant discrepancies.

The structure of the RAF is based on specific indicators called Key Risk Indicators (KRI) that measure the solvency of the Bank in the following areas:

- Share capital;
- Liquidity;
- Quality of the receivables portfolio;
- Profitability;
- Other specific risks the Bank is exposed to.

Target levels, consistent with the plan's defined values, the level I thresholds, defined as "warning" thresholds, that trigger discussion at Risks Management Committee level and subsequent communication to the Board of Directors and the level II thresholds, that required direct discussion in the Board of Director's Meeting to determine the actions to be taken are associated with the

various key ratios.

The I and II level thresholds are defined with scenarios of potential stress with respect to the plan's objectives and on dimensions having a clear impact for Banca Sistema. Starting from 1 January 2014, the Bank used an integrated reference framework both to identify its own risk appetite and for the internal process entailing the determination of the capital adequacy (Internal Capital Adequacy Assessment Process - ICAAP).

Furthermore, the Internal Capital Adequacy Assessment Process allows the Bank to comply with the public disclosure obligation, with appropriate tables, concerning its capital adequacy, to risk exposure and to the general characteristics of the management, control, and monitoring systems of the risks themselves, (the so-called "third pillar"). As concerns this matter, the Bank fulfils the public disclosure requirements with the issuing of Circular no. 285 of 17 December 2013 "Prudential supervisory provisions for banks" in which the Bank of Italy transposed the Directive 2013/36/EU (CRD IV) of 26 June 2013. This regulation, together with that contained in (EU) Regulations no. 575/2013 (the so-called "CRR") incorporates the standards defined by the Basel Committee on Banking Supervision (the so-called "Basel III").

1. General aspects

The prudential supervisory provisions, provide for the banks the possibility to determine the weighting coefficients for the calculation of the capital requirement with respect to credit exposure within the standardised approach based on the creditworthiness ratings issued by External Credit Assessment Institutions (ECAI) of the Bank of Italy.

Banca Sistema, as at 31 December 2016, uses the appraisal issued by the ECAI "DBRS", for the exposures to Central Authorities, and Public Sector Institutions and Entities, whereas, as concerns the valuations relative to the regulatory business segment, it uses the agency "Fitch Ratings Ltd".

The identification of a reference ECAI does not represent in any way, in subject matter or in purposes, an assessment on the merit of the opinions made by the

ECAI or a support of the methodologies used, for which the External Credit Assessment Institutions remain solely responsible.

The assessments issued by the rating agencies do not exhaust the creditworthiness assessment process that the Group performs with regard to its customers; rather they represent a further contribution to define the information framework regarding the credit quality of the customer. The satisfactory appraisal of the borrower's creditworthiness, with regards to capital and income, and of the correct remuneration of the risk, are made based on documentation acquired by the Bank; the information acquired from the Bank of Italy Central Credit Bureau and from other infoproviders, both when decisions are made during the subsequent monitoring, complete the informational framework.

For Banca Sistema, Credit risk is one of the Group's main components of overall exposure; the composition of the credit portfolio predominantly consists of National Institutions of the Public Administration, such local health authorities / Hospitals, Territorial entities (Regions, Provinces and Municipalities) and Ministries that, by definition, entail a very limited default risk.

The main components of Banca Sistema Group's operations that generate credit risk are:

- Factoring activities (with and without recourse);
- Loans to SMEs (with guarantee from the National Guarantee Fund – FNG);
- Acquisition without recourse of salary-/pension-backed loans;

During the third quarter of 2016, the Bank evaluated the impact of an ECAI DBRS downgrade of Italy (from A- to BBB) prior to that decision being made on 13 January 2017. From the analysis and as was later demonstrated, the main consequence of the deterioration of the country's creditworthiness was a reduction in the collateral given on refinancing transactions that did not have any particular effect on the level of the Bank's liquidity.

2. Credit Risk Management Policies

2.1 Organizational aspects

Banca Sistema's organizational model envisages that the preliminary credit assessment procedure be performed

carefully in accordance with the decision-making powers reserved to the decision-making bodies.

In order to maintain high credit quality in its loan portfolio, the Bank, as the Parent Company, deemed it expedient to concentrate all phases relative to the assumption and control of risk control upon its internal structures, thus obtaining, through the specialization of resources and the segregation of functions at each decision-making level, a degree of standardisation in the granting of credit and robust monitoring of the individual positions.

As mentioned above, the Bank's "Underwriting Office" performs the analyses for the granting of credit. The Office performs assessments focused on the separate analysis and extension of credit to counterparties (assignor, debtor) and on this takes place in all normal phases of the credit process, summarized as follows:

- "analysis and assessment": the gathering of quantitative and qualitative information from the counterparties under examination the system allows an opinion of the subject's reliability and is helpful in quantifying the proposed line of credit;
- "deliberation and formalisation": once the proposal has been deliberated upon, the contractual documentation to be signed by the counterparty is prepared;
- "monitoring the relationship": the continuous control of the counterparties benefiting from the credit allows any anomalies to be identified and consequentially prompt intervention.

Credit risk is mainly generated by a direct result of the definitive acquisition of credit from the customer company versus the insolvency of the assigned debtor. In particular, the credit risk generated by the factoring portfolio essentially consists of Institutions Public Administration.

In reference to each credit acquired, Banca Sistema performs, via the Collection Department, activities described further on in order to verify the credit status, and whether or not there are any impediments to the payment of the invoices to be assigned, and date scheduled for the payment thereof.

Specifically, the structure endeavours:

- to verify that each credit is certain, liquid and collectable, i.e. there are not disputes or complaints and that there is no further request for clarification or information with regards to said credit and should there be any, that said requests are promptly satisfied;
- to verify that the debtor has received and recorded in its system the relative deed of assignment, i.e. is aware that the credit has been assigned to Banca Sistema;
- to verify that the debtor, where provided for by the assignment agreement and by the purchase offer, has formalised its acceptance of the assignment of the relative credit or has not rejected it within the terms of the law;
- to verify that the debtor received all the documentation required to proceed with the payment (copy of invoice, orders, bills, transportation documents, etc.) and that had it recorded the corresponding debt in its system (existence of the credit);
- to verify c/o the local and/or regional institutions: the existence of specific allocations, available cash;
- to verify the payment status of the credits via meetings c/o the Public Administrations and/or debtor agencies, tele-phone contacts, emails, etc. in order to facilitate the ascertainment and the removal of any obstacles that could delay and/or impede payment.

With reference to other business: regarding the Loans to SME product, credit risk is associated with the inability of the two counterparties involved in the loan to honour their financial commitments i.e.:

- the debtor (SME);
- the Guarantee Fund (the Government of Italy).

The type of loan follows the usual operating process concerning the preliminary assessment, the disbursement and the monitoring of the credit. In particular, two separate due-diligence procedures are performed on this type of loan (one by the Bank and the other by Medio Credito Centrale, the so-called MCC) on the borrower of funds.

The debtor's insolvency risk is mitigated by direct (i.e. that referring to an individual exposure), explicit, unconditional and irrevocable guarantee by the Guarantee Fund, the sole Manager of which is "MCC".

As regards, instead, the acquisition of salary-/pension-backed loan portfolios, the credit risk is associated with the inability of the three counterparties involved in the loan process to honour their financial commitments, i.e.:

- the Employer (ATC)
- the financial assigning company
- the Insurance Company

The insolvency risk of Employer/ debtor is generated in the following cases:

- default of Employer (e.g.: bankruptcy);
- the debtor losing his job (e.g.: resignation/ dismissal of the debtor) or reduction of remuneration (e.g.: redundancy fund);
- death of the debtor.

The cases of risk described above are mitigated by the mandatory subscription of a life and employment insurance policies. In detail:

- the employment risk policy fully covers any insolvency deriving from the reduction of the debtor's remuneration whereas, for default by the Employer, the coverage is limited to the portion of the residual debt in excess of the termination indemnity accrued;
- the life risk policy anticipates that the insurance company will intervene to cover the portion of the residual debt expiring subsequent to death; any instalments previously not settled remain instead incumbent upon by the heirs.

The Bank is subject to the insolvency risk of the Insurance Company in the event that a claim is made upon a loan.

In order to mitigate this risk, the Bank requires that the outstanding credit portfolio be insured by several insurance companies observing following terms:

- an individual company with no rating or with rating less than Investment Grade may insure a maximum of 30% of the cases;
- an individual company of Investment Grade may insure a maximum of the 40% of the cases.

The Employer insolvency risk is generated in the event

that a case is retroceded back to the Employee, which must therefore, repay the credit to the Bank. The Framework Agreement initialled with the employer anticipates the possibility of retroceding the credit in the cases of fraud on the part of the Employer/debtor or in any case, of non-observance, on the part of the employer, of the assumptive criteria anticipated by the framework agreement.

As concerns the financial instruments held on its own account, the Bank performs security purchase transactions regarding Italian government debt, which are allocated, for prudential supervision purposes, in the banking book.

With reference to aforementioned operations the Bank identified and selected specific IT applications to manage and monitor the treasury limits on the securities portfolio and to set up the second level controls.

The Treasury Department, operating within the limits allowed by the Board of Directors, conducts said operations.

Also, with reference to the new regulatory framework, specifically to Circular no. 285 and to the respective Supervisory Bulletin no. 12 of December 2013, paragraph II.6 in matters of own funds, the Bank adhered to the extension of the prudential treatment of the profits and of the losses not realized, relative to the exposure to the Central Authorities classified in the "available-for-sale financial assets" category for the entire period provided for by art. 467(2), last paragraph of the CCR.

2.2 Management, measurement and control systems

The Bank sets effective Credit Risk Management as a strategic objective via instruments and process integrated to ensure a correct credit management in all phases (processing, disbursement, monitoring and management, intervening on loans with credit quality problems).

By involving the various Central structures of Banca Sistema and through the specialization of the resources and the separation of functions at each decision-making level, it seeks to guarantee a high degree of efficiency and standardisation in overseeing credit risk and monitoring the individual positions.

With specific reference to the monitoring of credit activities, the Bank, via the collection meetings, assesses and inspects the credit portfolio based upon the guidelines defined within the “collection policy”. The framework relative to the above credit risk ex-post management sets the objective of promptly identifying any anomalies and/or discontinuities and evaluating the persistence of risk profiles, in-line with the strategic indications provided.

The purchase activities of government securities classified among available-for-sale financial assets continued during 2015 in relation to the credit risk associated with the bond securities portfolios. Said financial assets, which in virtue of their classification fall within the perimeter of the “banking book” although outside of the bank’s traditional investment activity, are sources of credit risk.

This risk consists in the issuer’s inability to redeem, upon maturity, all or part of the bonds subscribed. The securities held by Banca Sistema consist exclusively of Italian government securities, with an average duration of less than a year for the overall portfolio. Furthermore, the formation of a portfolio of readily liquidatable assets is also expedient for anticipating the trend of the prudential regulations in relation to the governance and management of liquidity risk. As concerns counterparty risk, Banca Sistema’s operations call for extremely prudent reverse repurchase and repurchase agreements being that Italian government securities are the predominant underlying instrument and the Compensation and Guarantee Fund is the predominant counterparty.

2.3 Credit Risk mitigation techniques

It should be noted that, as of the balance-sheet date, the Bank did not implement any hedging of the credit portfolio.

As concerns credit and counterparty risk on the AFS portfolio and on the repurchase agreements, risk mitigation is pursued by a careful management of the operational autonomy, establishing limits in terms of both responsibility and the consistency and composition of the portfolio by type of securities.

2.4. Non-performing financial assets

The Banca Sistema Group defined its credit quality policy as a function of the provisions in the Bank of Italy Circular 272 (Accounts matrix), the principle definitions of which are provided on the following pages.

The Supervisory Provisions for Banks assign to intermediaries specific obligations concerning the monitoring and classification of loans: “The obligations of the operating units in the monitoring phase of the loan granted must be deducible from the internal regulation. In particular, intervention terms and methods must be set in case of irregularity. The measurement, management and classification criteria for irregular loans, as well as the related responsible units, must be set with resolution of the board of directors, which indicates the methods of coordination among these criteria and the methods required by the supervisory reports. The board of directors must be regularly informed on the performance of the irregular loans and the related recovery procedures.”

According to the definitions in the above-mentioned Bank of Italy Circular, financial assets that lie within the categories of the bad loans, unlikely to pay or non-performing past due and/or overdrawn exposures are defined as non-performing.

Exposures whose anomalous situation is attributable to factors relevant to the so-called “country risk” are the “non-performing” financial assets.

In particular, the following definitions apply:

Bad loans

On- and off-balance sheet exposures (loans, securities, derivatives, etc.) owed by a party in state of insolvency (even if not judicially ascertained) or in broadly similar situations, regardless of any loss forecast formulated by the Group (cf. art. 5 bankruptcy law). The definition therefore applies regardless of the existence of any collateral (real or private) provided as protection against the exposures.

This class also includes:

- the exposure to local institutions (municipalities and provinces) in state of financial difficulty for the portion subject to the applicable liquidation procedure;

- the credits purchased from third parties having bad parties as the primary obligator, regardless of the accounting portfolio in which it is allocated.

Unlikely to pay

Classification into this category is first of all the result of the Banks opinion regarding the improbability that, without recourse to actions such as the enforcement of the guarantee, the debtor will fulfil all of his credit obligations (principal and/or interest). This assessment is made independently of whether any sums (or instalments) are past due and not paid. It is therefore unnecessary to wait for explicit symptoms of irregularity (non-repayment) if there are elements that entail a situation of default risk on the part of the debtor (e.g. a crisis in the industrial sector in which the debtor operates).

The set of on- and off-balance sheet exposures to the same debtor in above conditions is named “unlikely to pay”, save that the conditions for classifying the debtor under bad loans do not exist.

Non-performing past due and/or overdrawn exposures

These are understood to be the on-balance sheet exposures at book value and “off-balance sheet” exposures (loans, securities, derivatives, etc.), other than those classified as bad loans, unlikely to pay, that, on the reference date of the report, are past due or have been overdrawn by more than 90 days. In order to verify the continuity of the overdue exposure in connection with the factoring operation, the following is specified:

- for “with recourse transactions”, the overdue exposure, other than that associated with the assignment of future credits, is determined only if both of the following conditions exist:
 - the advance is of an amount equal to or greater than amount of the credit coming due;
 - at least one invoice has not been honoured (past due) by more than 90 days and the set of the past due invoices (including those by less than 90 days) exceeds 5% of the total receivables;
- for “without recourse transactions”, for each assigned debtor, individual invoice that with the

greatest delay must be referred.

In the calculation of the capital requirement for the credit and counterparty risk, Banca Sistema uses the standardised approach. This envisages that the exposures that lie within the portfolios relative to “Central Authorities and Central Banks”, “Territorial entities”, and “Public sector institutions” and “Businesses”, must apply the notion of overdue and/or overdrawn exposures at the level of the debtor party.

The regulation also requires the overall exposure to a debtor to be recognised as past-due and/or overdrawn if, at the reference date of the report, the relevance threshold of 5% is exceeded.

Forborne exposures

Defined as forborne exposures (“forbearance”) are the exposures which lie in the categories of “Non-performing exposures with forbearance measures” and “Forborne performing exposures” as defined in the International Technical Standards (ITS).

A forbearance measure represents a concession towards a debtor which faces or is about to face difficulties in fulfilling its financial obligations (“financial difficulties”); a “concession” indicates one of the following actions:

- an amendment of the previous terms and conditions of a contract which the debtor is considered unable to fulfil due to its financial difficulties, that would not have been granted if the debtor was not in financial difficulty;
- a total or partial refinancing operation of a problem loan that would not have been granted if the debtor was not in financial difficulty.

Art. 172 of ITS EBA sets some situations which, if occurring, lead in any case to the presence of forbearance measures, i.e. when:

- an amended contract was classified as non-performing and would have been so in the absence of the amendment;
- the amendment made to the contract implies a partial or total cancellation of the debt;
- the intermediary approves the use of forbearance clauses incorporated in the contract for a debtor

classified as non-performing or that would have been so without resorting to these clauses;

- at the same time or close to the additional granting of credit by the intermediary, the debtor makes payments of capital or interest on another contract with the intermediary that was classified as non-performing or that would have been classified so in the absence of the refinancing.

According to these criteria, forbearance is presumed to have taken place when:

- the amended contract has totally or partially expired for more than 30 days (without being classified as non-performing) at least once during the three months before the amendment or would

have been so in the absence of the amendment;

- at the same time or close to the additional granting of credit by the intermediary, the debtor make payments of capital or interest on another contract with the intermediary that was totally or partially expired for more than 30 days (without being classified as non-performing) at least once during the three months before the amendment or would have been so in the absence of the amendment;
- the intermediary approves the use of forbearance clauses incorporated in the contract for a debtor which has expired for more than 30 days or that would have been so without resorting to these clauses.

QUANTITATIVE INFORMATION

A. CREDIT QUALITY

A.1 Non-performing and performing credit exposures: amounts, value adjustments, dynamics, economic and regional distribution

A.1.1 Distribution of the credit exposures by portfolios and by credit quality (book values)

Portfolios/quality	Bad loans	Unlikely to pay	Non-performing past due exposures	Performing past due exposures	Performing financial assets	Total
1. Financial assets available for sale	-	-	-	-	507,872	507,872
2. Financial assets held to maturity	-	-	-	-	-	-
3. Due from banks	-	-	-	-	83,493	83,493
4. Loans to customers	22,969	16,163	68,172	240,990	1,000,036	1,348,330
5. <i>Financial assets at fair value through profit and loss</i>	-	-	-	-	-	-
6. Financial assets held for disposal	-	-	-	-	-	-
Total 2016	22,969	16,163	68,172	240,990	1,591,401	1,939,695
Total 2015	13,899	5,093	65,255	258,961	2,042,290	2,385,468

A.1.2 Distribution of credit exposures by portfolio and by credit quality (gross and net values)

Portfolios/quality	Non-performing assets			Performing financial assets			Total (net exposure)
	Gross exposure	Specific adjustments	Net exposure	Gross exposure	Specific adjustments	Net exposure	
1. Financial assets available for sale	-	-	-	570,872	-	570,872	507,872
2. Financial assets held to maturity	-	-	-	-	-	-	-
3. Due from banks	-	-	-	83,493	-	83,493	83,493
4. Loans to customers	123,760	16,456	107,304	1,246,868	5,842	1,241,025	1,348,330
5. Financial assets at fair value through profit and loss	-	-	-	-	-	-	-
6. Financial assets held for disposal	-	-	-	-	-	-	-
Total 2016	123,760	16,456	107,304	1,838,233	5,842	1,832,390	1,939,695
Total 2015	91,353	7,137	84,216	2,299,485	3,233	2,296,252	2,380,468

A.1.2.1 Distribution of credit exposures by portfolios

Portfolios/seniority past due	OTHER EXPOSURES					Total (net exposure)
	Past due up to 3 months	Past due by more than 3 months up to 6 months	Past due by more than 6 months up to 1 year	Past due by more than 1 year	Not past due	
1. Financial assets available for sale	-	-	-	-	507,872	507,872
2. Financial assets held to maturity	-	-	-	-	-	-
3. Due from banks	-	-	-	-	83,493	83,493
4. Loans to customers	51,872	28,800	67,505	92,813	1,000,035	1,241,025
5. Financial assets at fair value through profit and loss	-	-	-	-	-	-
6. Financial assets held for disposal	-	-	-	-	-	-
Total 2016	51,872	28,800	67,505	92,813	1,591,400	1,832,390
Total 2015	163,710	27,445	43,308	24,497	2,037,292	2,296,252

A.1.3 On- and off-balance sheet credit exposures to banks: gross and net values

Type of exposures/Values	Gross exposure				Performing financial assets	Individual adjustments	Collective adjustments	Net exposure
	Non-performing assets							
	Up to 3 months	from more than 3 months up to 6 months	from more than 6 months up to 1 year	Performing financial assets				
A. ON-BALANCE SHEET EXPOSURES	-	-	-	-	-	-	-	-
a) Bad loans	-	-	-	-	-	-	-	-
of which: forborne exposures	-	-	-	-	-	-	-	-
b) Unlikely to pay	-	-	-	-	-	-	-	-
of which: forborne exposures	-	-	-	-	-	-	-	-
c) Non-performing past due exposures	-	-	-	-	-	-	-	-
of which: forborne exposures	-	-	-	-	-	-	-	-
d) Performing past due exposures	-	-	-	-	-	-	-	-
of which: forborne exposures	-	-	-	-	-	-	-	-
e) Other performing exposures	-	-	-	-	83,493	-	-	83,493
of which: forborne exposures	-	-	-	-	-	-	-	-
TOTAL A	-	-	-	-	83,493	-	-	83,493
B. OFF-BALANCE-SHEET EXPOSURES	-	-	-	-	-	-	-	-
a) Non-performing	-	-	-	-	-	-	-	-
b) Performing	-	-	-	-	-	-	-	-
TOTAL B	-	-	-	-	-	-	-	-
TOTAL (A+B)	-	-	-	-	83,493	-	-	83,493

A.1.4 On-balance sheet credit exposures to banks: dynamics of gross non-performing exposures

On-balance sheet exposures to Banks are all performing.

A.1.5 On-balance sheet credit exposures to banks: dynamics of overall adjustments

There are no non-performing exposures to banks.

A.1.6 On- and off-balance sheet credit exposures to customers: gross and net values

Type of exposures/Values	Gross exposure				Performing financial assets	Individual adjustments	Collective adjustments	Net exposure
	Non-performing assets							
	Up to 3 months	from more than 3 months up to 6 months	from more than 6 months up to 1 year	More than one year				
A. ON-BALANCE SHEET EXPOSURES								
a) Bad loans	1	62	352	34,816	-	12,260	-	22,971
of which: forborne exposures	-	-	-	-	-	-	-	-
b) Unlikely to pay	11,867	2,869	2,063	3,390	-	4,027	-	16,163
of which: forborne exposures	-	-	-	-	-	-	-	-
c) Non-performing past due exposures	29,665	8,916	11,100	18,661	-	170	-	68,172
of which: forborne exposures	-	2,811	-	-	-	-	-	-
d) Performing past due exposures	-	-	-	-	241,350	-	552	240,798
of which: forborne exposures	-	-	-	-	-	-	-	-
e) Other performing exposures	-	-	-	-	1,513,390	-	5,290	1,508,099
of which: forborne exposures	-	-	-	-	-	-	-	-
TOTAL A	41,533	11,847	13,515	56,867	1,754,720	16,457	5,842	1,856,203
B. OFF-BALANCE-SHEET EXPOSURES	-	-	-	-	-	-	-	-
a) Non-performing	-	-	-	-	-	-	-	-
b) Performing	-	-	-	-	45	-	-	45
TOTAL B	-	-	-	-	45	-	-	45
TOTAL (A+B)	41,533	11,847	13,515	56,867	1,754,785	16,457	5,842	1,856,248

A.1.7 On-balance sheet credit exposures to customers: dynamics of gross non-performing exposures

Reasons/Categories	Bad loans	Unlikely to pay	Non-performing past due exposures
A. Starting gross exposure	20,021	5,913	65,420
of which: non-derecognized assigned exposures			
B. Increases	34,903	26,249	148,037
B.1 incoming performing exposures	11,213	13,984	101,309
B.2 transfers from others categories of non-performing exposures	13,964	3,569	-
B.3 other increases	9,726	8,251	44,848
Business combination transactions		445	1,880
C. Decreases	19,693	11,973	145,115
C.1 outgoing performing exposures	4,724	-	58,529
C.2 derecognitions	-	10	-
C.3 collections	14,969	2,389	79,655
C.4 gains on sales	-	-	-
C.5 losses from disposal	-	-	-
C.6 transfers to others categories of non-performing exposures	-	9,574	6,931
C.7 other decreases	-	-	-
D. Final gross exposure	35,231	20,189	68,342
of which: non-derecognized assigned exposures			

A.1.8 On-balance sheet credit exposures to customers: dynamics of overall adjustments

Reasons/Categories	BAD LOANS		UNLIKELY TO PAY		NON-PERFORMING PAST DUE EXPOSURES	
	Total	Of which: forborne exposures	Total	Of which: forborne exposures	Total	Of which: forborne exposures
A. Initial total adjustments	6,122	-	820	-	194	-
of which: non-derecognized assigned exposures	-	-	-	-	-	-
B. Increases	8,491	-	4,071	-	136	-
B.1 value adjustments	7,690	-	3,771	-	59	-
B.2 losses from disposal	-	-	-	-	-	-
B.3 transfers from others categories of non-performing exposures	722	-	5	-	-	-
B.4 other increases	79	-	45	-	77	-
Business combination transactions			250			
C. Decreases	2,353	-	865	-	162	-
C.1 valuation write-backs	2,107	-	98	-	110	-
C.2 collection write-backs	1	-	-	-	32	-
C.3 profits from disposals	-	-	-	-	-	-
C.4 derecognitions	-	-	-	-	-	-
C.5 transfers to others categories of non-performing exposures	-	-	45 722	-	5	-
C.6 other decreases	245	-	-	-	15	-
D. Final total adjustments	12,260	-	4,026	-	168	-
of which: non-derecognized assigned exposures	-	-	-	-	-	-

A.2 CLASSIFICATION OF THE EXPOSURES BASED ON EXTERNAL AND INTERNAL RATING

A.2.1 Distribution of on- and off-balance sheet credit exposures by external rating class

The risk categories for the external rating indicated in this table refer to the creditworthiness classes of the debtors/ guarantors pursuant to prudential requirements (cf. Circular no. 285 of 2013 “Regulations for the supervision of banks” and subsequent updates).

The Bank uses the standardised approach in accordance with the risk mapping of the rating agencies:

- “DBRS Ratings Limited”, for exposures to: central authorities and central banks; supervised brokers; public sector in-stitutions; territorial entities.

Exposures	External rating class						Without rating	Total
	Class 1	Class 2	Class 3	Class 4	Class 5	Class 6		
A. On-balance sheet exposures	-	-	-	-	-	-	1,836,184	1,836,184
B. Derivatives	-	-	-	-	-	-	-	-
B.1 Financial derivatives	-	-	-	-	-	-	-	-
B.2 Credit derivatives	-	-	-	-	-	-	-	-
C. Guarantees given	-	-	-	-	-	-	45	45
D. Commitments to disburse funds	-	-	-	-	-	-	-	-
E. Other	-	-	56,586	-	-	-	-	56,586
Total	-	-	56,586	-	-	-	1,836,229	1,892,815

of which long-term rating

Creditworthiness class	Risk weighting factors				ECAI
	Central authorities and central banks	Supervised brokers, public sector institutions and territorial entities	Multilateral development banks	Companies and other parties	DBRS Ratings Limited
1	0%	20%	20%	20%	da AAA a AAL
2	20%	50%	50%	50%	da AH a AL
3	50%	100%	50%	100%	da BBBH a BBBL
4	100%	100%	100%	100%	da BBH a BBL
5	100%	100%	100%	150%	da BH a BL
6	150%	150%	150%	150%	CCC

of which short-term ratings (for exposures to supervised brokers)

Creditworthiness class	Risk weighting factors	ECAI
		DBRS Ratings Limited
1	20%	R-1 (high), R-1 (middle), R-1 (low)
2	50%	R-1 (high), R-2 (middle), R-2 (low)
3	100%	R-3
4	150%	R-4, R-5
5	150%	
6	150%	

“Fitch Ratings”, for exposures to companies and other parties.

of which long-term rating

Creditworthiness class	Risk weighting factors				ECAI
	Central authorities and central banks	Supervised brokers, public sector institutions and territorial entities	Multilateral development banks	Companies and other parties	Fitch Ratings
1	0%	20%	20%	20%	from AAA to AA-
2	20%	50%	50%	50%	from A+ to A-
3	50%	100%	50%	100%	from BBB+ to BBB-
4	100%	100%	100%	100%	from BB+ to BB-
5	100%	100%	100%	150%	from B+ to B-
6	150%	150%	150%	150%	CCC+ and lower

of which short-term ratings (for exposures to supervised brokers)

Creditworthiness class	Risk weighting factors	ECAI
		Fitch Ratings
1	20%	F1+F2
2	50%	F2
3	100%	F3
from 4 to 6	150%	less than F3

A.3 Distribution of guaranteed credit exposures by type of Guarantee

A.3.2 Banking group - Credit exposures to guaranteed customers

	Net exposure	Real security (1)				CLN	Personal security (2)						Total (1)+(2)		
		Mortgaged estate	Properties under financial lease	Securities	Other collateral		Credit derivatives			Credit commitments					
							Governments and Central Banks	Other public institutions	Banks	Other subjects	Governments and Central Banks	Other public institutions		Banks	Other subjects
2. Guaranteed on-balance sheet credit exposures:	348,600	-	-	9,292	-	-	-	-	-	62,372	213	-	8,559	343,898	
2.1 fully guaranteed	319,991	-	-	9,291	-	-	-	-	-	38,683	-	-	8,559	319,991	
- of which non-performing	6,540	-	-	-	-	-	-	-	-	6,021	-	-	518	6,540	
2.2 partially guaranteed	28,609	-	-	1	-	-	-	-	-	23,689	213	-	-	23,907	
- of which non-performing	4,930	-	-	-	-	-	-	-	-	4,578	-	-	-	4,578	
2. Guaranteed off-balance sheet credit exposures:	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
2.1 fully guaranteed	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
- of which non-performing	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
2.2 partially guaranteed	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
- of which non-performing	-	-	-	-	-	-	-	-	-	-	-	-	-	-	

DISTRIBUTION AND CONCENTRATION OF CREDIT EXPOSURES

A.1 Banking group - Distribution by sector of On- and off-balance sheet credit with customers (book value)

Exposures/Counterparties	Governments			Other public institutions			Financial companies			Insurance companies			Non-financial companies			Other subjects		
	Net Exposure	Individual adjustments	Collective adjustments	Net Exposure	Individual adjustments	Collective adjustments	Net Exposure	Individual adjustments	Collective adjustments	Net Exposure	Individual adjustments	Collective adjustments	Net Exposure	Individual adjustments	Collective adjustments	Net Exposure	Individual adjustments	Collective adjustments
A. On-balance sheet exposures																		
A.1. Bad loans	-	-	-	10,240	5,137	-	-	-	-	-	-	-	12,573	6,543	-	156	582	-
of which: forbome exposures	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
A.2 Unlikely to pay	-	-	-	-	-	-	-	-	-	-	-	-	15,208	4,024	-	955	2	-
of which:	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
forbome exposures	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
A.3 Non-performing past due exposures	736	-	-	49,743	130	-	-	-	-	1	-	-	17,196	38	-	497	1	-
of which: forbome exposures	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
A.4 Performing exposures	744,220	-	108	496,715	-	6,132	2,223	-	2	-	-	238,564	-	-	1,689	267,173	-	641
of which:	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
forbome exposures	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
TOTAL A	744,956	-	108	556,698	5,267	6,132	2,223	-	3	-	-	283,540	10,605	1,689	268,781	585	641	-
B. Off-balance-sheet exposures																		
B.1. Bad loans	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
B.2. Unlikely to pay	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
B.3. Other non-performing assets	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
B.4. Performing exposures	-	-	-	-	-	-	-	-	-	-	-	9	-	-	-	36	-	-
TOTAL B	-	-	-	-	-	-	-	-	-	-	-	9	-	-	36	-	-	-
TOTAL (A+B) 2016	744,956	-	108	556,698	5,267	6,132	2,223	-	3	-	-	283,549	10,605	1,689	268,817	585	641	-
TOTAL (A+B) 2015	1,195,995	20	108	563,893	4,934	1,436	198,608	-	-	-	-	291,438	1,616	1,147	129,130	562	546	-

B.2 Banking group - Territorial distribution of the on-balance sheet credit exposures and off-balance sheet credit exposures to customers to customers (book value)

Exposures/Geographical Areas	ITALY		OTHER EUROPEAN COUNTRIES		AMERICA		ASIA		REST OF THE WORLD	
	Net Exposure	Total value adjustments	Net Exposure	Total value adjustments	Net Exposure	Total value adjustments	Net Exposure	Total value adjustments	Net Exposure	Total value adjustments
A. On-balance sheet exposures										
A.1 Bad loans	22,971	12,260	-	-	-	-	-	-	-	-
A.2 Unlikely to pay	16,163	3,817	-	-	-	-	-	-	-	-
A.3 Non-performing past due exposures	68,172	170	-	-	-	-	-	-	-	-
A.4 Other performing exposures	1,737,662	8,540	9,609	25	1,625	5	-	-	-	-
Total	1,844,968	24,787	9,609	25	1,625	5	-	-	-	-
B. Off-balance-sheet exposures										
B.1 Bad loans	-	-	-	-	-	-	-	-	-	-
B.2 Unlikely to pay	-	-	-	-	-	-	-	-	-	-
B.3 Other non-performing assets	-	-	-	-	-	-	-	-	-	-
B.4 Other performing exposures	45	-	-	-	-	-	-	-	-	-
Total	45	-	-	-	-	-	-	-	-	-
Total (A+B) 2016	1,845,013	24,787	9,609	25	1,625	5	-	-	-	-
Total (A+B) 2015	2,359,118	10,311	21,211	59	-	-	-	-	-	-

Exposures/Geographical Areas	NORTH WEST Italy		NORTH EAST Italy		CENTRAL Italy		SOUTHERN Italy and the ISLANDS	
	Net Exposure	Total value adjustments	Net Exposure	Total value adjustments	Net Exposure	Total value adjustments	Net Exposure	Total value adjustments
A. On-balance sheet exposures								
A.1 Bad loans	3,818	1,641	957	863	3,491	2,155	14,703	7,600
A.2 Unlikely to pay	1,812	222	-	-	1,570	38	12,780	3,557
A.3 Non-performing past due exposures	2,559	8	955	2	12,796	36	51,862	124
A.4 Other performing exposures	200,920	804	92,981	344	861,194	1,340	582,571	6,054
Total	209,109	2,675	94,893	1,209	879,051	3,569	661,915	17,335
B. Off-balance-sheet exposures	-	-	-	-	-	-	-	-
B.1 Bad loans	-	-	-	-	-	-	-	-
B.2 Unlikely to pay	-	-	-	-	-	-	-	-
B.3 Other non-performing assets	-	-	-	-	-	-	-	-
B.4 Other performing exposures	36	-	-	-	9	-	-	-
Total	36	-	-	-	9	-	-	-
Total (A+B) 2016	209,145	2,675	94,893	1,209	879,060	3,569	661,915	17,335
Total (A+B) 2015	164,498	1,014	63,497	788	1,472,179	1,574	658,943	6,935

B.3 Banking group - Territorial distribution of the on-balance sheet credit exposures and off-balance sheet credit exposures to banks (book value)

Exposures/Geographical Areas	ITALY		OTHER EUROPEAN COUNTRIES		AMERICA		ASIA		REST OF THE WORLD	
	Net Exposure	Adjustments overall value	Net Exposure	Adjustments overall value	Net Exposure	Adjustments overall value	Net Exposure	Adjustments overall value	Net Exposure	Adjustments overall value
A. On-balance sheet exposures										
A.1 Bad loans										
A.2 Unlikely to pay										
A.3 Non-performing past due exposures										
A.4 Other performing exposures	83,493									
Total A	83,493									
B. Off-balance-sheet exposures										
B.1 Bad loans										
B.2 Unlikely to pay										
B.3 Other non-performing assets										
B.4 Other performing exposures										
Total B										
Total (A+B) 2016	83,493									
Total (A+B) 2015	2,121									

B.4 Major exposures

As at 31 December 2016, the Parent Company's major exposures are as follows:

- a) Book value €1,204,797 (in thousands)
- b) Weighted value €89,077 (in thousands)
- c) Number 18

E. OPERAZIONI DI CESSIONE

A. Financial assets assigned and not fully derecognized

QUALITATIVE INFORMATION

The financial assets sold and not derecognized refer predominantly to Italian government securities used for repurchase agreements. Said financial assets are classified in the financial statements among the available-for-sale financial assets, while the repurchase agreement loan is presented in due to customers.

As a last resort the financial assets sold and not derecognized comprise trade receivables used for loan transactions in the ECB (Abaco).

E.1. Banking group - Financial assets sold and not cancelled: book value and entire value

Technical forms/Portfolio	Financial assets held for trading			Financial assets at fair value through profit and loss			Financial assets available for sale			Financial assets held to maturity			Due from banks			Loans to customers			Total	
	A	B	C	A	B	C	A	B	C	A	B	C	A	B	C	A	B	C	31/12/2016	31/12/2015
A. Non-derivative financial assets	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	498,718	878,574
1. Debt securities	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	295,528	771,332
2. Equity securities	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3. UCI	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4. Loans	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	203,190	107,242
B. Derivative instruments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total 2016	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	498,718	-
<i>of which non-performing</i>	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total 2015	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	878,574
<i>of which non-performing</i>	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

Key:

A = financial assets disposed of and recorded in whole (book value)

B = financial assets disposed of and recorded partially (book value)

C = financial assets disposed of and recorded in partially (entire value)

E.2. Banking group - Financial liabilities against financial assets sold and not derecognized: book value

Liabilities/Asset portfolio	Financial assets held for trading	Financial assets at fair value through profit and loss	Financial assets available for sale	Financial assets held to maturity	Due from banks	Loans to customers	Total
1. Due to customers	-	-	295,581	-	-	-	295,581
a) against fully recorded assets	-	-	295,581	-	-	-	295,581
b) against partially recorded assets	-	-	-	-	-	-	-
2. Due to banks	-	-	-	-	-	-	-
a) against fully recorded assets	-	-	-	-	-	-	-
b) against partially recorded assets	-	-	-	-	-	-	-
Total 2016	-	-	295,581	-	49,257	-	295,581
Total 2015	-	-	761,966	-	49,257	30,603	841,826

F. BANKING GROUP - MODELS FOR THE MEASUREMENT OF CREDIT RISK

1.2 Banking group - market risks

Banca Sistema did not conduct trading activity on financial instruments. As at 31 December 2015, no active positions are recorded in the trading book for regulatory purposes that might generate market risks.

The existing limit system defines a careful and balanced management of the operational autonomy, establishing limits in terms of portfolio amounts and composition by type of security.

1.2.1 Interest rate risk and price risk - regulatory trading portfolio

QUALITATIVE INFORMATION

The trading risk moved exclusively following the trading of a security; due to the size of the investment the price risk is limited.

1.2.2 Interest rate risk and price risk - Regulatory Trading Portfolio

QUALITATIVE INFORMATION

A. General aspects, management procedures and methods of measuring the interest rate risk and the price risk

Interest rate risk is defined as the risk that the financial assets/liabilities record an increase /decrease in value because of movements contrary to the interest rate curve. The Bank identified the sources that generate interest rate risk with reference to the credit processes and to the Bank's collection.

The Bank calculates the exposure to interest rate risk on the banking book consistent as dictated by regulations currently in force, via the simplified regulatory approach (Cf. Circular no. 285/2006, Part one, Title III, Chapter 1, Schedule C); by using this method, the Bank is able to monitor the impact of the unexpected changes in market

conditions on shareholders' equity, in this way identifying the relative mitigation measures to be implemented.

In greater detail, the processes of estimating the exposure to interest rate risk of the banking book anticipated by the simplified method is organized in the following phases:

- Determination of the relevant currencies. "Relevant currencies" are considered those that represent a portion of total assets, or also of the banking book liabilities, greater than 5%. For the purposes of the methodology for calculating exposure to interest rate risk, the positions denominated in "relevant currencies" are considered individually, while the position in "non-relevant currencies" are aggregated for the relative exchange value in Euro;
- Classification of the assets and liabilities in time brackets. 14 time brackets are defined. The fixed-rate assets and liabilities are classified based on their residual maturity, while those at floating-rates based on the interest rate renegotiation date. Specific classification rules are prescribed for specific assets and liabilities. With particular reference to the deposit and savings product "Si conto! Deposito", the Bank proceeded with the bucketization that takes into account the implied redemption option.
- Weighting the net exposures of each bracket. The asset and liability positions are offset within each bucket, obtaining a net position. The net position by bracket is multiplied by the corresponding weighting factor obtained as the product between a hypothetical change of the rates and an approximation of the modified duration for the individual bracket;
- Sum of the weighted net exposures of the various brackets. The weighted exposures calculated for each bracket (sensitivity) are summed together. The net weighted exposure thus obtained approximates the change of the present value of the posting, denominated in a certain currency, in the event of

the assumed rate shock;

- Aggregation in the various currencies. The absolute values of the exposures regarding the individual “relevant currencies” and the aggregate of the “non-relevant currencies” are summed together, obtaining a value that represents the change of the economic value of the Bank as a function of the assumed rate trends.

With reference to the Bank’s financial assets, the main sources that generate interest rate risk are Loans to customers and the bond securities portfolio. As concerns the financial liabilities, relevant instead are the customer deposits and savings activities via current accounts, the savings account, and the collections on the interbank market.

Given the foregoing submissions, it should be noted that:

- the interest rates applied to the factoring customers are at a fixed rate and can also be modified unilaterally by the Bank, (in compliance with regulations in force and existing contracts);
- the average financial term of the bond securities portfolio is a less than one year;
- the salary/pension-backed loan that contains fixed rate contract is that with the greatest duration, however on the balance-sheet date this portfolio

is contained and it is not deemed expedient to perform Interest rate hedging operations on said maturities;

- the REPO deposits c/o the Central bank are of short duration (the maximum maturity is equal to 3 months);
- The customers’ deposits on the deposit account product are at a fixed rate for the entire duration of the constraint, which can be unilaterally renegotiated by the Bank in compliance with regulations in force and the existing contracts);
- the REPO and reverse REPO agreements are generally of short duration, without prejudice to different funding needs.

The Bank continuously monitors the main asset and liability postings subject to interest rate risk, furthermore, no hedging instruments were uses as at the balance sheet date.

B. Fair value hedges

The Bank did not perform any such transactions in 2016.

C. Cash flow hedging

The Bank did not perform any such transactions in 2016.

QUANTITATIVE INFORMATION

Banking book: distribution by residual term (by repricing date) of financial assets and liabilities

Type/Residual term	on demand	up to 3 months	from more than 3 months to 6 months	from more than 6 months up to 1 year	from more than 1 years up to 5 years	from more than 5 years up to 10 years	more than 10 years	Unspecified term
1. Non-derivative financial assets	415,666	327,112	229,568	461,202	365,715	139,566	866	-
1.1 Debt securities	-	92,140	100,092	295,597	20,043	-	-	-
- with option of advance repayment	-	-	-	-	-	-	-	-
- other	-	92,140	100,092	295,597	20,043	-	-	-
1.2 Loans to banks	76,313	6,854	326	-	-	-	-	-
1.3 Loans and advances to customers	339,353	228,118	129,150	165,605	345,672	139,566	866	-
- current accounts	12,253	-	-	-	-	1	-	-
- other loans	327,100	228,118	129,150	165,605	345,672	139,565	866	-
- with option of advance repayment	10,104	34,649	29,199	29,299	201,059	122,581	15	-
- other	316,996	193,469	99,951	136,306	144,613	16,984	851	-
2. Cash liabilities	489,098	673,731	82,972	75,596	476,423	4,733	8,026	-
2.1 Due to customers	468,822	358,731	70,887	75,596	283,346	4,733	8	-
- current accounts	468,392	60,168	65,678	64,613	236,904	3,768	8	-
- other payables	430	298,563	5,209	10,983	46,442	965	-	-
- with option of advance repayment	-	-	-	-	-	-	-	-
- other	430	298,563	5,209	10,983	46,442	965	-	-
2.2 Due to banks	20,276	315,000	-	-	122,850	-	-	-
- current accounts	-	-	-	-	-	-	-	-
- other payables	20,276	315,000	-	-	122,850	-	-	-
2.3 Debt securities	-	-	12,085	-	70,227	-	8,018	-
- with option of advance repayment	-	-	12,085	-	-	-	-	-
- other	-	-	-	-	70,227	-	8,018	-
2.4 Other liabilities	-	-	-	-	-	-	-	-
- with option of advance repayment	-	-	-	-	-	-	-	-
- other	-	-	-	-	-	-	-	-
3. Financial derivatives	-	594	41	84	415	-	-	-
3.1 With underlying security	-	-	-	-	-	-	-	-
- Options	-	-	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-	-	-
- Other derivatives	-	-	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-	-	-
3.2 Without underlying security	-	594	41	84	415	-	-	-
- Options	-	594	41	84	415	-	-	-
+ long positions	-	27	41	84	415	-	-	-
+ short positions	-	567	-	-	-	-	-	-
- Other derivatives	-	-	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-	-	-
4. Other off-balance-sheet transactions	-	-	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-	-	-

1.2.3 Exchange rate risk

QUALITATIVE INFORMATION

A. General aspects, management processes and methods of measuring the foreign exchange risk

All postings are in euro, except for the security in the trading portfolio.

The exchange rate risk is limited due to the size of the investment.

1.2.4 Derivative instruments

A. Financial derivatives

The Bank does not operate on own account with derivative instruments.

B. Credit derivatives

As at 31 December 2016, the Bank had not executed any derivative contract to hedge the credit portfolio.

B.2 OTC Credit derivatives: gross positive fair value - breakdown by product

Items	CURRENCY					
	US DOLLARS	GB POUNDS	YEN	CANADIAN DOLLARS	SWISS FRANCS	OTHER CURRENCIES
A. Financial assets	-	-	-	-	-	2,962
A.1 Debt securities	-	-	-	-	-	-
A.2 Equities	-	-	-	-	-	2,962
A.3 Loans to banks	-	-	-	-	-	-
A.4 Loans to customers	-	-	-	-	-	-
A.5 Other financial assets	-	-	-	-	-	-
B. Other assets	-	-	-	-	-	-
C. Financial liabilities	-	-	-	-	-	-
C.1 Due to banks	-	-	-	-	-	-
C.2 Due to customers	-	-	-	-	-	-
C.3 Debt securities	-	-	-	-	-	-
C.4 Other financial liabilities	-	-	-	-	-	-
D. Other liabilities	-	-	-	-	-	-
E. Financial derivatives	-	-	-	-	-	-
- Options	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-
- Other derivatives	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-
Total assets	-	-	-	-	-	2,962
Total liabilities	-	-	-	-	-	-
Difference (+/-)	-	-	-	-	-	2,962

C. FINANCIAL AND CREDIT DERIVATIVES

As at 31 December 2016 the item shows no amount.

1.3 Banking group - liquidity risk

QUALITATIVE INFORMATION

A. General aspects, management processes and methods of measuring liquidity risk

Liquidity risk is represented by the possibility that the Bank is unable to maintain its payment commitments due to the inability to procure funds or to the inability to sell assets on the market to manage the financial imbalance. It is also represented by the inability to procure adequate new financial resources, in terms of amount and cost, with respect to operational need/advisability, that forces the Bank to slow or stop the development of activity, or to incur excessive funding costs to deal with their commitments, with significant negative impacts on the profitability of the its activity.

The financial sources are represented by capital, by funding from customers, from the funds procured on the domestic and international interbank market as well from the Eurosystem.

To monitor the effects of the intervention strategies and to limit the liquidity risk, the Bank identified a specific section dedicated to monitoring the liquidity risk in the Risk Appetite Framework (RAF).

Furthermore, in order to promptly detect and manage any

difficulties in procuring the funds necessary to conduct its activity, every year, Banca Sistema, consistent with the prudential supervisory provisions, updates its liquidity policy and Contingency Funding Plan, i.e. the set of specific intervention strategies in case of liquidity stress, anticipating the procedure to procure funds in the event of an emergency.

This set of strategies is of fundamental importance to attenuate liquidity risk.

The aforesaid policy defines, in terms of liquidity risk, the objectives, the processes and the intervention strategies in case of liquidity stress, the organizational structures responsible for implementing the interventions, the risk indicators, the relevant calculation method and warning thresholds, and procedures to procure the funding sources that can be used in case of emergency.

During 2015, the Bank continued to adopt a particularly conservative financial policy meant to stabilize funding. This approach, allowed a balanced distribution between inflows from retail customer and corporate and institutional counterparties.

As of today, the financial resources available are satisfactory for the current and forward looking volumes of activity. The Bank is continuously active ensuring a coherent development, always in-line with the composition of its financial resources.

In particular, Banca Sistema, prudentially, has constantly maintained a high quantity of securities and readily liquid assets to cover all of the deposits and savings products oriented towards the retail segment.

QUANTITATIVE INFORMATION

1. Time distribution of financial assets and liabilities by remaining contractual term

Item/Time brackets	on demand	from more than 1 day to 7 days	from more than 7 day to 15 days	from more than 15 days to 1 month	from more than 1 month to 3 months	from more than 3 months to 6 months	from more than 6 months up to 1 year	from more than 1 year up to 5 years	Over 5 years	Unspecified term
Non-derivative financial assets	399,746	26,538	3,587	50,021	216,361	245,577	449,890	375,680	131,857	6,835
A.1 Government securities	-	-	-	-	92,042	100,086	295,396	20,018	-	-
A.2 Other debt securities	-	-	-	-	-	-	-	-	-	-
A.3 UCI units	-	-	-	-	-	-	-	-	-	-
A.4 Loans	399,746	26,538	3,587	50,021	124,319	145,491	154,494	355,662	131,857	6,835
- banks	8,497	-	-	11	8	330	-	-	-	6,835
- customers	391,249	26,538	3,587	50,010	124,311	145,161	154,494	355,662	131,857	-
Cash liabilities	483,513	415,619	39,183	24,126	196,318	77,489	85,836	480,811	24,741	-
B.1 Deposits and current accounts	481,400	48,040	38,978	22,955	195,291	65,991	65,264	236,904	3,776	-
- banks	20,276	45,000	35,000	15,000	150,000	-	-	-	-	-
- customers	461,124	3,040	3,978	7,955	45,291	65,991	65,264	236,904	3,776	-
B.2 Debt securities	-	-	-	-	-	1,314	1,314	70,000	20,000	-
B.3 Other liabilities	2,113	367,579	205	1,171	1,027	10,184	19,258	173,907	965	-
Off-balance-sheet transactions	-	-	-	-	-	-	-	-	-	-
C.1 Financial derivatives with exchange of capital	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-
C.2 Financial derivatives without exchange of capital	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-
C.3 Deposits and loans receivable	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-
C.4 Irrevocable commitments to disburse funds	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-
C.5 Financial guarantees issued	-	-	-	-	-	-	-	-	-	-
C.6 Financial Guarantees received	-	-	-	-	-	-	-	-	-	-
C.7 Credit derivatives with exchange of capital	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-
C.8 Credit derivatives without exchange of capital	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-

With reference to the financial assets subject to retained securitisation, at the end of 2016, Banca Sistema entered into two securitisation transactions in which it had subscribed to all the securities issued.

1.4 Banking Group - operational risks

QUALITATIVE INFORMATION

Operational risk is the risk of loss arising from inadequate or dysfunctioning internal processes, human resources or systems, or from external events. This type of risk includes - among other things - the ensuing losses from fraud, human errors, business disruption, unavailability of systems, breach of contract, and natural catastrophes. Operational risk, therefore, refers to other types of events that, under present conditions, would not be individually relevant if not analysed jointly and quantified for the entire risk category.

A. General aspects, management processes and methods of measuring operational risk

In order to calculate the internal capital generated by the operational risk, the Bank adopts the Basic Indicator Approach, which provides for the application of a regulatory coefficient (equal to 15%) to the three-year average of the relevant indicator defined in Article 316 of EU Regulation no. 575/2013 of 26 June 2013. The above-said indicator is given by the sum (with sign) of the following elements:

- interest income and similar revenue;
- interest expense and similar expense;
- income on shares, quotas and other variable/fixed yield securities;
- income for commissions/fees;
- expenses for commissions/fees;
- profit (loss) from financial transactions;
- other operating income.

Consistent with that anticipated by the relevant legislation, the indicator is calculated gross of provisions and operating expenses; also excluded from computation are:

- profits and losses on the sale of securities not included in the trading portfolio;
- income deriving from exceptional or irregular items;
- income deriving from insurance.

As of 2014, the Bank measured the operating risks

events via a qualitative performance indicator (IROR - Internal Risk Operational Ratio) defined within the operational risk management and control process (ORF - Operational Risk Framework). This calculation method allows a score to be defined between 1 and 5, inclusive (where 1 indicates a low risk level and 5 indicates a high risk level) for each event that generates an operational risk.

The Bank assesses and measures the level of the identified risk, also in consideration also the controls and of the mitigating actions implemented. This method requires a first assessment of the possible associated risks in terms of probability and impact (so-called "Gross risk level") and a subsequent analysis of the existing controls (qualitative assessment on the effectiveness and efficiency of the controls) which could reduce the gross risk, on the basis of which specific risk levels (the so-called "Residual risk") are determined. Finally, the residual risks are mapped on a predefined scoring grid, useful for the subsequent calculation of IROR via appropriate aggregation of the scores defined for the individual operational procedure.

Moreover, the Bank assesses the operational risk associated with the introduction of new products, activities, processes and relevant systems mitigating the onset of the operational risk via a preliminary evaluation of the risk profile.

The Bank places strong emphasis on possible ICT risks. The Information and Communication Technology (ICT) risk is the risk of incurring economic, reputational and market losses in relation to the use of information and communication technology. In the supplemented representation of the business risks, this type of risk is considered, in accordance with the specific aspects, among operational, reputational and strategic risks.

The Bank monitors the ICT risks based on the continuous information flows between the functions concerned defined in its IT security policies.

To protect the integrity of data, the Bank has implemented a datawarehouse; this tool allows the Bank to have a single repository that guarantees the correctness, completeness and accuracy of the data, as well as the possibility for a single point of access port

to the information within the Bank. In order to conduct consistent and complete analysis with respect to the other activities conducted by the Bank's other control functions, the results in relation to the non-compliance risk audits conducted by the Compliance and Anti-money laundering function, are shared both within the Risk Management and Compliance Department, with the Internal Audit and Risk Management Committee, and with the CEO. The Internal Audit Department also monitors the regular performance of bank operations and processes and evaluates the level of effectiveness and efficiency of the overall internal control system set up to deal with risk exposure.

Finally, as an additional protection against operational

risk, the Bank has:

- insurance coverage on the operational risks deriving from actions of third parties or procured to third parties. In order to select the insurance coverage, the Bank initiated specific assessment activities, with the support of a primary market broker, to identify the best offers in terms of price/conditions proposed by several insurance undertakings;
- appropriate contractual riders to cover damages caused by of infrastructure and service suppliers;
- a business continuity plan;
- the assessment of each operational procedure in effect, in order to define the controls implemented to protect against risk activities.

PART F - INFORMATION ON CONSOLIDATED SHAREHOLDERS' EQUITY

SECTION 1 - CONSOLIDATED SHAREHOLDERS' EQUITY

A. QUALITATIVE INFORMATION

The objectives pursued in the Group's equity management are inspired by the prudential supervisory provisions, and are oriented towards maintaining adequate levels of capitalisation to take on risks typical to credit positions.

The income allocation policy aims to strengthen the Group's capital with special emphasis on primary capital, to the prudent distribution of the operating results, and to guaranteeing a correct balance of the financial position.

B. QUANTITATIVE INFORMATION

B.1 Consolidated shareholders' equity: analysis by type of company

As at 31 December 2016, the Shareholders' equity was composed as follows:

Items/Values	31/12/2016	31/12/2015
1. Share capital	9,651	9,651
2. Share premium reserve	39,352	39,436
3. Reserves	39,608	26,314
4. Equity instruments	-	-
5. (Treasury shares)	(52)	-
6. Valuation reserves	425	350
- Financial assets available for sale	680	417
- Property and equipment	-	-
- Intangible assets	-	-
- Hedges of foreign investments	-	-
- Cash flow hedges	-	-
- Foreign exchange differences	-	-
- Non-current assets held for sale	-	-
- Actuarial gain (loss) relative to defined-benefit plans	(255)	(67)
- Quotas of the valuation reserves regarding investee companies valued at equity	-	-
- Special revaluation laws	-	-
7. Profit (loss) for the year	25,313	17,607
Total	114,296	93,358

B.2 Valuation reserves for financial assets available for sale: breakdown

Assets/Values	31/12/2016		31/12/2015	
	Positive reserve	Negative reserve	Positive reserve	Negative reserve
1. Debt securities	221	-	508	113
2. Equity securities	458	-	-	-
3. Units of UCI	-	-	-	-
4. Loans	-	-	-	-
Total	679	-	508	113

B.3 Valuation reserves for financial assets available for sale: annual changes

	Debt securities	Equity securities	Units of UCI	Loans
1. Opening balance	395	-	-	-
2. Positive variations	558	-	-	-
2.1 Increases in fair value	330	630	-	-
2.2 Reclassifications from negative reserves to the income statement:	-	-	-	-
▪ following impairment	22	-	-	-
▪ following disposal	-	-	-	-
2.3 Other changes	22	-	-	-
3. Negative variations	732	-	-	-
3.1 Reductions in fair value	206	55	-	-
3.2 Adjustments for impairment losses	-	-	-	-
3.3 Reclassifications of positive reserves to the income statement: following disposal	-	-	-	-
3.4 Other changes	623	-	-	-
3.4 Other changes	109	227	-	-
4. Closing balance	221	458	-	-

SECTION 2 - OWN FUNDS AND CAPITAL RATIOS FOR BANKS

The Parent company's own funds and capital ratios are shown below.

2.1 Own funds

A. QUALITATIVE INFORMATION

Own Funds, risk weighted assets and solvency ratios as at 31 December 2016 were determined based on the

new regulation, harmonised for Banks, contained in the Directive 2013/36/EU (CRD IV) and in the Regulation (EU) 575/2013 (CRR) of 26 June 2013, that transpose in the European Union the standards defined by the Basel Committee on Banking Supervision (the so-called Basel 3 framework), and based upon the Circular of the Bank of Italy no. 285 and no. 286 (enacted in 2013),

and the update of Circular no. 154.

The legislative provisions relative to own funds require the gradual introduction of the new regulatory framework, through a transitory period, in general until 2017, during which certain elements that under normal circumstances will be computable or fully deductible in the Common Equity, impact the Common Equity Tier 1 capital only by percentage.

Own funds are characterized by a 3-tier structure as follows:

1) Common Equity Tier 1, CET1 capital, composed of:

A) Common Equity Tier 1 - CET1, which includes:

- Paid up capital of €9.7 million;
- A share-premium reserve of €39.4 million;
- Other reserves including undistributed profits of €59 million

In particular, this item includes a net profit of €19 million recognized in Own funds pursuant to article 26 of the CRR, net of foreseeable dividends pertaining to the Group and of the other positive accumulated income components of €425 thousand composed as follows:

- Negative reserve for actuarial losses deriving from defined benefit plans in accordance with the application of the new IAS 19 amounting to €255 thousand;
- Positive reserves on available-for-sale assets amounting to €680 thousand.

D) Items to be deducted from CET1 that include:

- Goodwill and other intangible assets, equal to €1.8 million;

E) Transitional regime - Impact on CET1 (+/-),

including the minority interest subject to temporary provisions.

This item includes the following temporary adjustments:

- The exclusion of unearned profits on AFS securities issued by Central Authorities, amounting to €221 thousand (-);
- A positive filter on negative actuarial reserves (IAS 19), amounting to €102 thousand (+);
- Application of the prudential filter for fair value profits, amounting to €184 thousand (-)

2) Additional Tier 2, AT1 capital, composed of:

G) Additional Tier1 (AT1) including elements to be deducted and the effects of the transitional provisions.

This item includes: the security ISIN IT0004881444 issued by Banca Sistema as an innovative tool of blended rate capital amounting to €8 million.

3) Tier 2, T2 capital, composed of:

M) Tier2 (T2) including elements to be deducted and the effects of the transitional provisions.

This item includes the security ISIN IT0004869712 issued by Banca Sistema as an ordinary subordinated loan (Lower Tier 2) equal to €12 million.

O) Positive filter originating from the application of national filters on the positive AFS reserve, pursuant to Circular 285/2013 amounting to €92 thousand (+).

B. QUANTITATIVE INFORMATION

	31/12/2016
A. Common Equity Tier 1 (CET1) before application of prudential filters	106,759
of which CET 1 instruments subject to transitional provisions	-
B. CET1 prudential filters (+/-)	-
C. CET1 including elements to be deducted and of the effects of the transitional provisions (A+/-B)	106,759
D. Items to be deducted from CET1	1,835
E. Transitional Provisions - Impact on CET (+/-)	(303)
F. Total Common Equity Tier 1 (CET1) (C-D+/-E)	104,621
G. Additional Tier1 (AT1) including elements to be deducted and the effects of the transitional provisions	8,000
of which AT1 instruments subject to transitional provisions	-
H. Items to be deducted from AT1	-
I. Transitional Provisions - Impact on AT1 (+/-)	-
L. Total Additional Tier 1 (AT1) (G-H+/-I)	8,000
M. Tier2 (T2) including elements to be deducted and the effects of the transitional provisions	12,000
of which T2 instruments subject to transitional provisions	-
N. Items to be deducted from T2	-
O. Transitional Provisions - impact on T2 (+/-)	92
P. Total Tier 2 (T2) (M-N+/-O)	12,092
Q. Total Own Funds (F+L+P)	124,713

2.2 Capital adequacy

A. QUALITATIVE INFORMATION

The Own funds totalled €124.7 million, against risk-weighted assets of €788 million, derived almost exclusively from credit risk.

Based on article 467(2) of the CRR, implemented by the Bank of Italy in Circular 285, the Bank adopted the option to exclude, from its own funds, the profits or losses not realized relative to the exposures to the Central

Authorities classified in the Available-for-sale financial assets (AFS) category. The effects of said exclusion on the capital ratios are marginal.

As at 31 December 2016, the Banca Sistema Group presented a CET1 capital ratio equal to 13.3%, a Tier 1 capital ratio equal to 14.3% and a Total capital ratio of 15.8%.

B. QUANTITATIVE INFORMATION

Categories/Values	UNWEIGHTED AMOUNTS		WEIGHTED AMOUNTS/REQUIREMENTS	
	31/12/2016	31/12/2015	31/12/2016	31/12/2015
A. RISK ASSETS				
A.1 Credit and counterparty risk	2,469,702	2,234,170	652,999	535,194
1. Standardised approach	2,469,702	2,234,170	652,999	535,194
2. Internal ratings based approach	-	-	-	-
2.1 Basic	-	-	-	-
2.2 Advanced	-	-	-	-
3. Securitised debt	-	-	-	-
B. MINIMUM REGULATORY REQUIREMENTS				
B.1 Credit and counterparty risk			52,240	42,815
B.2 Credit assessment adjustment risk			-	-
B.3 Settlement risk			-	-
B.4 Market risk			368	-
1. Standard approach			368	-
2. Internal models			-	-
3. Concentration risk			-	-
B.5 Operational risk			10,436	8,037
1. Basic indicator approach			10,436	8,037
2. Standardised approach			-	-
3. Advanced measurement approach			-	-
B.6 Other calculation elements			-	-
B.7 Total capital requirements			63,043	50,853
C. RISK ASSETS AND CAPITAL RATIOS			788,041	635,658
C.1 Risk-weighted assets			788,041	635,658
C.2 CET1 capital/risk-weighted assets (CET1 capital ratio)			13.28%	13.67%
C.3 Tier1 capital/risk-weighted assets (Tier 1 capital ratio)			14.29%	14.93%
C.4 Total own funds/risk-weighted assets (Total Capital Ratio)			15.83%	16.82%

PART G - BUSINESS COMBINATION TRANSACTIONS INVOLVING COMPANIES OR BUSINESS LINES

Section 1 - Transactions completed during the year

On 1 July 2016, the acquisition of 100% of Beta Stepstone S.p.A. was finalised for final consideration of €56.7 million, net of various contractual reductions and adjustments of €3.5 million.

During the acquisition process, the amount of late payment interest receivable not yet collected by Beta

was placed in an escrow account, release of which to the seller is conditional solely on the collection of that late payment interest, fully securing the receivable in question.

Key information regarding this transaction is summarised below:

Company name	Transaction date (1)	Transaction costs	Interest %	Net banking income (2)	Group net income (2)
Beta Stepstone S.p.A.	1 July 2016	56,7 mln	100%	84,198	26,412

(1) Date control was acquired and the date from which the economic results of Beta were included

(2) The value, as set out in IFRS 3, were determined assuming that the business combination transaction had taken place at the start of the year.

Section 2 - Transactions completed after the close of the financial year

The Group did not enter into any business combination transactions after the close of the year or until the date these financial statements were prepared.

PART H - TRANSACTIONS WITH RELATED PARTIES

Transactions with related parties and connected parties, including the relative authorisation and disclosure procedures, are governed by the 'Procedure governing transactions with associated parties' approved by the Board of Directors and published on the internet site of the Parent Company, Banca Sistema S.p.A..

Transactions between the Group companies and related parties or connected parties were carried out in the interest of the Company, including within the scope of ordinary operations; these transactions were carried out in accordance with market conditions and, in any event, on the basis of mutual financial advantage and in compliance with all procedures.

Transactions with parties who exercise management and control functions in accordance with art. 136 of the Consolidated Law on Banking have been included in the

Executive Committee resolution, specifically authorised by the Board of Directors and with the approval of the Statutory Auditors, until 4 July 2016, which is the date of abrogation of the mentioned Committee, subject to compliance with the obligations provided under the Civil Code with respect to matters relating to the conflict of interest of directors.

Pursuant to IAS 24, the related parties of Banca Sistema include:

- shareholders with significant influence;
- companies belonging to the banking Group;
- companies subject to significant influence;
- key management personnel;
- the close relatives of key management personnel and the companies controlled by (or connected with) such personnel or their close relatives.

DISCLOSURE ON THE COMPENSATION OF KEY MANAGEMENT PERSONNEL

The following data show the compensation of key managers, as per IAS 24 and Bank of Italy Circular no. 262 of 22 December 2005 as subsequently updated, which requires the inclusion of the members of the Board of Statutory Auditors.

Values in thousands of Euro	BOARD OF DIRECTORS	BOARD OF STATUTORY AUDITORS	OTHER EXECUTIVES	31/12/2016
Remuneration to Board of Directors and Board of Statutory Auditors	1,298	70	-	1,368
Short-term benefits for employees	-	-	1,962	1,962
Post-employment benefits	49	-	195	260
Other long-term benefits	-	-	-	-
Termination benefits	-	-	-	-
Share-based payments	-	-	-	-
Total	1,347	70	2,157	3,590

DISCLOSURE ON TRANSACTIONS WITH RELATED PARTIES

The following table shows the assets, liabilities, guarantees and commitments as at 31 December 2016, differentiated by type of related party with an indication of the impact on each individual caption.

Values in thousands of Euro	SUBSIDIARIES	DIRECTORS, BOARD OF STATUTORY AUDITORS AND KEY MANAGERS	OTHER RELATED PARTIES	% OF CAPTION
Loans to customers	19,723	655	9,463	2.2%
Due to customers	14,295	1,559	5,540	1.7%
Securities issued	-	-	20,102	22.3%
Other assets	-	-	12	0.1%
Other liabilities	138	-	-	0.2%

The following table indicates the costs and income for 2016, differentiated by type of related party.

Values in thousands of Euro	SUBSIDIARIES	DIRECTORS, BOARD OF STATUTORY AUDITORS AND KEY MANAGERS	OTHER RELATED PARTIES	% OF CAPTION
Interest income	107	2	9	0.1%
Interest expenses	45	48	62	1.0%
Other administrative expenses	458	-	-	2.0%
Fee and commission income	-	-	1,209	11.1%
Fee and commission expense	47	-	-	3.4%

The following table sets forth the details of each related party.

	AMOUNT (Thousands of Euro)	PERCENTAGE (%)
ASSETS	29,186	1.46%
Loans to customers		
CS Union S.p.A.	9,463	0.75%
Speciality Finance Trust Holdings Ltd	1,157	0.09%
Largo Augusto Servizi e Sviluppo S.r.l.	18,566	1.47%
LIABILITIES	39,755	1.99%
Due to customers		
CS Union S.p.A.	12	0.00%
Beta Stepstone S.p.A.	14,295	1.13%
Shareholders - SGBS	4	0.00%
Shareholders - Fondazione Pisa	4,282	0.34%
Shareholders - Fondazione CR Alessandria	842	0.07%
Shareholders - Fondazione Sicilia	80	0.01%
Other liabilities		
Speciality Finance Trust Holdings Ltd	138	0.23%
Securities issued		
Shareholders - Fondazione Pisa	20,102	22.25%

	AMOUNT (Thousands of Euro)	PERCENTAGE (%)
REVENUES	1,325	
Interest income		
CS Union S.p.A.	61	0.07%
Speciality Finance Trust Holdings Ltd	45	0.05%
Shareholders - Fondazione CR Alessandria	1	0.00%
Shareholders - Fondazione Pisa	7	0.01%
Fee and commission income		
Shareholders - Fondazione Pisa	1,209	11.10%
COSTS	1,813	
Interest expenses		
CS Union S.p.A.	20	0.13%
Shareholders - Fondazione Pisa	1,244	0.19%
Beta Stepstone S.p.A.	45	0.30%
Fee and commission expense		
Beta Stepstone S.p.A.	47	3.37%
Other administrative expenses		
Speciality Finance Trust Holdings Ltd	458	2.03%

PART I - PAYMENT AGREEMENTS BASED ON OWN EQUITY INSTRUMENTS

During FY 2016, the Bank did not conduct the transactions under discussion.

Disclosure of the consideration paid to the auditing company

Pursuant to the provisions of art. 149 duodecies of the Consob Issuers' Regulations, the information regarding the fees paid to the auditing company KPMG S.p.A. and to the companies affiliated with the same network are reported below for the following services:

1. Auditing services that include:
 - The auditing of the annual accounts, for the purpose of expressing a professional opinion.
 - The auditing of the interim accounts.
2. Certification services that include tasks whereby the auditor evaluates a specific element, the determination of which is performed by another

party who is responsible thereof, through appropriate criteria, in order to express a conclusion that provides the recipient party a confidence level concerning said specific element.

3. Tax advisory services.
4. Other services.

The fees presented in the table, pertaining to 2016, are those contracted out, including any index-linking (but not out-of-pocket expenses, of any regulatory contribution and VAT). They do not include, in accordance with the cited provision, the compensation recognized to any secondary auditors or to parties of the respective networks.

Type of services	Entity providing the service	Addressee	Remuneration
Audit of the Financial statements and Quarterly Reports of listed companies	KPMG S.p.A.	Banca Sistema S.p.A.	184
Audit of the Financial statements	KPMG S.p.A.	LASS S.r.l.	14
Total			198

PART L - SEGMENT REPORTING

For the purposes of segment reporting as per IFRS 8, the income statement is broken down by segment as follows.

Breakdown by segment: profit and loss data at 31 December 2016

Items	31/12/2016			
	Factoring	Banking	Corporate	Consolidated total
<i>Values in thousands of Euro</i>				
Interest margin	61,318	8,791	890	71,000
Net fee and commission income	9,153	462	(555)	9,060
Other costs/revenue	-	-	1,423	1,423
Net interest and other banking income	70,471	9,253	1,758	81,483
Net value adjustments due to loan impairment	(4,293)	(5,472)	-	(9,765)
Net income from banking activities	66,178	3,781	1,758	71,718

Breakdown by segment: balance sheet data as at 31 December 2016

Items	31/12/2016			
	Factoring	Banking	Corporate	Consolidated total
<i>Values in thousands of Euro</i>				
Financial assets	-	-	515,834	515,834
Due from banks	-	-	83,493	83,493
Due to banks	-	-	458,126	458,126
Loans to customers	986,169	345,222	16,938	1,348,329
Due to customers	50,547	-	1,211,576	1,262,123

The Factoring division includes the business area related to the origination of trade and tax receivables with and without recourse. In addition, the division includes the business area related to the management and recovery of receivables on behalf of third parties.

The Banking segment includes the business area related to the origination of guaranteed loans to small and medium-sized enterprises, pension- and salary-backed loan portfolios and costs/income from assets under

administration and the placement of third-party products.

The Corporate segment includes activities related to the management of the Group's financial resources and costs/income in support of the business activities. Moreover, this segment includes all the consolidation entries, as well as all the inter-company cancellations.

The secondary disclosure by geographic area has been omitted as immaterial, since the customers are mainly concentrated in the domestic market.

CERTIFICATION OF THE CONSOLIDATED CONDENSED FINANCIAL REPORT
IN ACCORDANCE WITH ARTICLE 81-TER OF CONSOB REGULATION
NO. 11971 OF 14 MAY 1999 AS AMENDED AND SUPPLEMENTED

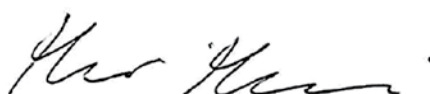
1. The undersigned, Gianluca Garbi, in his capacity as CEO, and Margherita Mapelli, in her capacity as Manager responsible for drafting the company accounting documents of Banca Sistema S.p.A. hereby certify, having taken into account the provisions of art. 154-bis, paragraphs 3 and 4, of Legislative Decree no. 58 of 24 February 1998:
 - the suitability as regards the characteristics of the company, and
 - that the Group has effectively applied the administrative and accounting procedures for preparing the Consolidated financial statements for the period from 1 January 2016 to 31 December 2016.
2. The suitability and effective application of the administrative and accounting process for the drafting of the consolidated financial statements as at 31 December 2016 was verified based on internally defined methodologies, consistent with the provisions of the reference standards for the internal audit system generally accepted on an international level.
3. Moreover, the undersigned hereby certify that:
 - 3.1 The consolidated financial statements:
 - a) have been prepared in accordance with the applicable international financial reporting standards recognised in the European Community pursuant to Regulation (EC) no. 1606/2002 of the European Parliament and of the Council of 19 July 2002;
 - b) correspond with the accounting books and records;
 - c) are suitable for providing a faithful and proper representation of the financial performance, income, and cash flows of the issuer and of the group of companies included in the consolidation.
 - 3.2 The Directors' Report contains a reliable analysis of the performance, operating results and financial situations of the issuer and of the companies included in the consolidation, together with a description of the main risks and uncertainties to which they are exposed.

Milano, 8 March 2017

Gianluca Garbi
Chief Executive Officer



Margherita Mapelli
*Designated manager responsible for drafting company
accounting documents*



INDEPENDENT AUDITORS'
REPORT



KPMG S.p.A.
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(Translation from the Italian original which remains the definitive version)

Independent auditors' report pursuant to articles 14 and 16 of Legislative decree no. 39 of 27 January 2010

To the shareholders of
Banca Sistema S.p.A.

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of the Banca Sistema Group (the "group"), which comprise the statement of financial position as at 31 December 2016, the income statement, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended and notes thereto.

Directors' responsibility for the consolidated financial statements

The parent's directors are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38/05 and article 43 of Legislative decree no. 136/15.

Independent auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with the International Standards on Auditing (ISA Italia) promulgated pursuant to article 11 of Legislative decree no. 39/10. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the bank's



preparation of consolidated financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the bank's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by directors, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the group's financial position as at 31 December 2016 and of its financial performance and cash flows for the year then ended in accordance with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38/05 and article 43 of Legislative decree no. 136/15.

Report on other legal and regulatory requirements

Opinion on the consistency of the directors' report and certain information presented in the report on corporate governance and ownership structure with the consolidated financial statements

We have performed the procedures required by Standard on Auditing (SA Italia) 720B in order to express an opinion, as required by the law, on the consistency of the directors' report and the information presented in the report on corporate governance and ownership structure required by article 123-bis.4 of Legislative decree no. 58/98, which are the responsibility of the parent's directors, with the consolidated financial statements. In our opinion, the directors' report and the information presented in the report on corporate governance and ownership structure referred to above are consistent with the consolidated financial statements of the Banca Sistema Group as at and for the year ended 31 December 2016.

Milan, 23 March 2017

KPMG S.p.A.

(signed on the original)

Bruno Verona
Director of audit

CONSOLIDATED
FINANCIAL STATEMENTS
AS AT
31 DECEMBER
2016

BANCA
SISTEMA
CONTEMPORARY BANK