BANKA KOPER

2016 Annual Report

Bank of INTESA SANPAOLO

ANNUAL REPORT 2016

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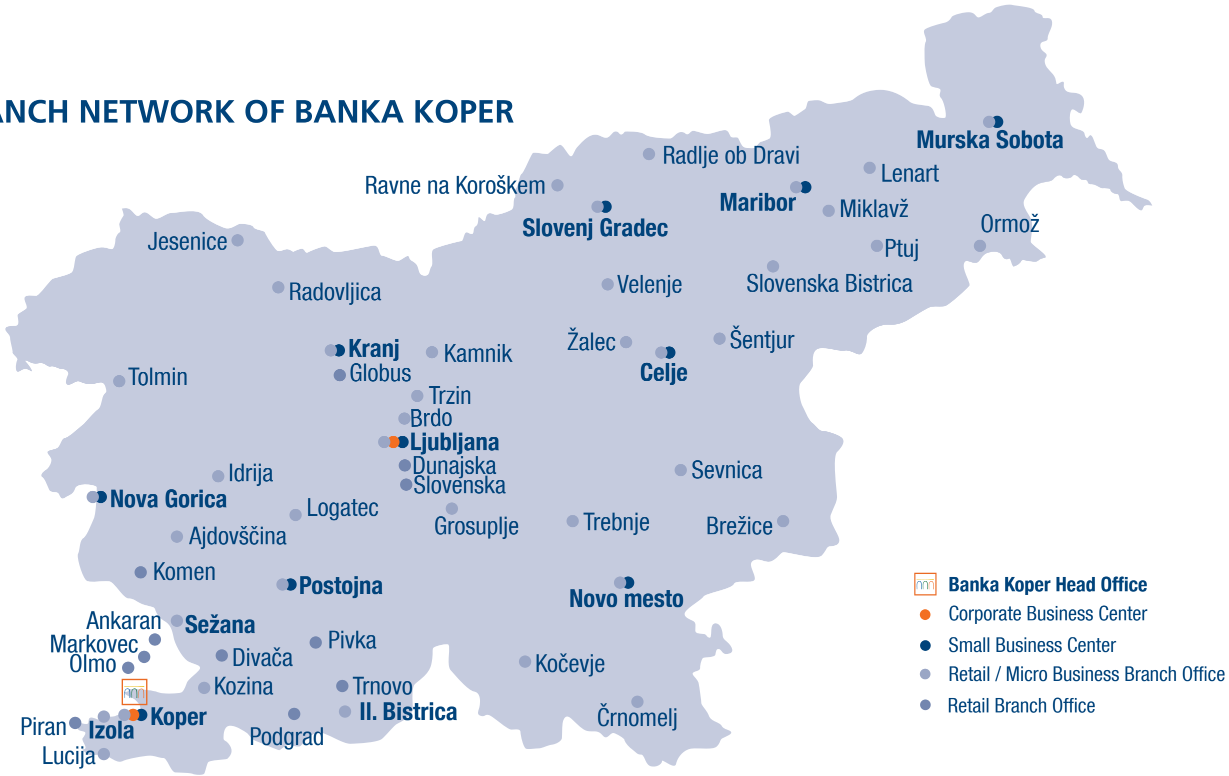
Business Report 2016

Banka Koper at a glance

BRANCH NETWORK OF BANKA KOPER



Banka Koper is a universal bank and among the seven largest Slovenian banks. It was founded more than sixty years ago, but its rapid growth began in the late 1990s when it developed from a local into a pan-Slovenian bank. Today, it has 52 branches in all the major Slovenian towns. Known as an innovative bank in the rapidly changing competitive landscape at home and abroad, Banka Koper provides designed to respond to changes in consumer needs and behaviour with regard to the delivery of bank services in key segments at the international level. Banka Koper is a member of Intesa Sanpaolo, the banking group formed by the merger of Banca Intesa and Sanpaolo IMI on 1 January 2007.

Shareholder structure of Banka Koper d. d.

Shareholder	Equity holding in per cent 31. 12. 2016	31. 12. 2015
Intesa Sanpaolo S. p. A.	98,9%	98,4%
Minority shareholders	1,1%	1,6%

Intesa Sanpaolo is one of the leading banking groups in the euro area and the leader in Italy in all business areas (retail, corporate, and wealth management). Thanks to its wide branch network in Italy – there are more than 4,000 branches – the Group offers a broad range of services to around 11.1 million customers. Its international operations cover Central and Eastern Europe, and Middle Eastern and North African countries. It has subsidiaries in 12 countries where approximately 1,200 branches offer products and services to 7.9 million customers. The international network offers support to companies across 29 countries.

International credit ratings

	2016	2015
Long-term rating	BBB	BBB
Short-term rating	F2	F2
Viability	bb	bb
Support	2	2

On 12 May 2016, FitchRatings London affirmed all ratings assigned to Banka Koper d.d. in 2015 The Long-term Issuer Default Rating (IDR) was affirmed at 'BBB', Short-term Issuer Default Rating was affirmed at 'F2', Viability Rating was affirmed at 'bb' and Support Rating at '2'.

According to FitchRatings, the ratings assigned to Banka Koper "are the strongest of Slovenian commercial banks in 2015 and reflect its asset quality and performance through the cycle, stable capital and funding profiles and strong risk controls and underwriting standards, benefiting from close integration with Intesa Sanpaolo S.p.A. (ISP)".

Milestones in the bank's corporate history

2016

As the first bank in Slovenia, Banka Koper introduced the contactless mobile payments with smartphones, enabled by the mobile wallet Wave2Pay, which is based on Host Card Emulation technology.

The announcement of the revamping of the Bank's operations in Slovenia and the change of its name to Intesa Sanpaolo Bank.

2015

The merger by absorption of the subsidiary Finor Leasing into the Bank's organisational structure.

As the first bank in Slovenia, Banka Koper has created a brand-new cashless payment service using smartphones and QR code technology.

2014

Launch of the mobile and internet banking – Banka IN for Businesses.

2013

Launch of the mobile banking - Banka IN for Individuals.

Beginning of the Inspire debit card issuing.

2012

Establishing of entrepreneurship centers for small businesses.

2011

The first green branch and introduction of electronic signing of bank transactions.

The exclusive issue of the American Express cards.

2008

The Bank launches a new online banking solution - Banka IN.

2007

Banka Koper became a member of Intesa Sanpaolo Group.

2005

Introduction of the first smart payment card.

2002

The bank joins the Sanpaolo IMI Group - its majority shareholder.

2001

Preparations for strategic alliance with the Sanpaolo IMI, S.p.A banking group, establishment of the Open-ended Mutual Pension Fund.

1998

The developement of the i-Net Banka internet banking solution.

1997

New name and a new corporate identity for Banka Koper.

1996

The branch network expands to other Slovenian regions.

1992

Withdrawal from the LB bank system and launch of the first Slovenian payment card - Activa.

1955

Foundation of Istrska komunalna the bank.

Management overview

1. REPORT OF THE MANAGEMENT BOARD

In the year 2016, the macroeconomic scenario for the Slovenian economy was characterized by a general improvement of the business cycle which was driven by the recovery of the GDP growth alongside with that of the employment and of the private consumption levels.

Despite these favourable conditions, domestic lending activity continued to show a stagnating dynamic, with only a notable exception for the housing and consumer loans segments. Over the course of the year, abundant liquidity and very low interest rates came out again as the main features defining the domestic banking environment.

All in all, these trends lead banks to engage in a fierce price-competition for the granting of loans and for the attraction of new customers. Aggressive re-financing propositions by competitor banks also emerged in managing banking relationships with creditworthy borrowing customers. As a consequence, the profitability of the banking sector was affected by a marked contraction of the contribution of lending margins. The lower cost of risk which ensued from the improvement of the quality of the banks' credit portfolio, however, compensated these unfavourable movements.

Against this backdrop, in 2016 Banka Koper managed to accomplish a successful performance, posting a growth of customer lending volumes and of profitability. Loan volumes especially picked up in the last quarter of the year, mainly owing to the clinching of a few long-term financing deals with large domestic corporates; volumes in the retail segment, conversely, showed a steady growth throughout the year, benefitting from the brisk activity in the mortgage market, namely in the fixed-rate housing loans segment.

The positive commercial performance of our bank was corroborated by the confirmation of a sound capital endowment CET1 Regulatory capital 257.19 million euros and capital ratio 17.40% and by a further enhancement of the quality of our assets. As to the latter, it is worth mentioning that the overall NPEs (non performing exposures) stock of the Bank was consistently reduced over the course of the year. Total amount of cash NPEs decreased by 31%, i.e. from 254 million euros to 176 million euros. Cash collections of bad loans, in particular, attained a significant result (28 million euros), matching the already positive outcome of workout initiatives recorded in 2015.

In 2016, in recognition of its resilient asset quality and performance, healthy liquidity and capital buffers, the bank was assigned a BBB (negative) rating by the FitchRatings agency, one more time the highest among the ratings received by Slovenian banks in the course of the year.

Yet another recognition of the banks' quality and positive perception came from a survey conducted by an independent agency comparing customer satisfaction levels among domestic peer banks. In accordance with the ECSI (European Customer Satisfaction Index) methodology, in the mid-2016 survey Banka Koper showed an ECSI index above that of selected domestic competitors, scoring notably good results in after sale, internet and mobile banking services.

The constant drive for innovation pursued by the bank over the last years was one of the main factors contributing to these results. Consistently with its past track-record of excellence in digital channels, in 2016 Banka Koper launched the new Wave2Pay mobile-wallet application with a view to allow the Bank's customers to execute safe and fast payments via compatible mobile devices.

With the support of the Innovation Center of our Parent Group, another innovative digital-business platform, Tech-marketplace, was set up by our Bank in the course of the year. Tech-marketplace is a solution specially designed for technology firms and start-ups, which is geared towards the creation of a digital market place where firms belonging to a specific industry or supply-chain may make their demand and supply meet.

Along this digital journey, in 2016 another important stage was the initiation of the extensive Big Financial Data project. The project originates from one of the largest and most far-reaching initiatives envisaged and designed at our Parent Group's level. Ensuring data quality and enhancing data management capacity of all the group's units are the main deliverables of this project, which will eventually empower our Bank with a state-of the-art tool for analytical, financial reporting, and, ultimately, customer-profiling purposes.

For our Bank, innovation is not only bound to technological solutions. A full commitment to innovative financial solutions is also part of our Bank's mission and a permanent pledge to our customers. As a tangible example of this commitment, in 2016 the Bank set up a new international trade-receivable financial program with one of the largest Slovenian exporters. The program features the securitization of export claims from the Slovenian manufacturer through a revolving financing scheme jointly set up by our Bank and Banca IMI, the specialized corporate and trade finance arm of the Intesa Sanpaolo group.

All the above prove the professional skills and the capacity of our Bank to timely adopt best banking practices. However, in a rapidly changing banking environment a constant effort to revise and tune-up our business model is a vital requirement. In this regard, during 2016 the Bank started to consider new marketing and strategic actions meant to strengthen the Bank's presence and image in some of the most promising areas of the Slovene banking industry, namely the corporate finance and the wealth management segments.

The envisaged future actions have received the support of our Parent Group and will benefit from the cooperation of some of the Group's subsidiaries operating in the target segments. In this framework, to mark the commitment of the Group towards Slovenia and its recognition of the positive achievements attained by our Bank, the Intesa Sanpaolo Group took the decision to rename of our Bank with the group brand. The Shareholding Assembly of the Bank thus passed the decision to rename the Bank to Banka Intesa Sanpaolo d.d. on the meeting held on the 19th of December of 2016.

The Management Board of the Bank acknowledges the motives and the appreciation underlying this decision, as well as the work and dedication of all the staff of Banka Koper who over the course of the years brought the Bank to the high regard that it presently enjoys with the Parent Group and all its stakeholders. These achievements, the vision and the strategic support for a new growth path shared with the Intesa Sanpaolo Group, make the Management Board confident about the future prospects of Banka Intesa Sanpaolo d.d. in Slovenia and reinforce its commitment towards the goal of an enhanced presence of our Group in this country.

2. REPORT OF THE SUPERVISORY BOARD

REPORT OF THE SUPERVISORY BOARD ON THE EXAMINATION OF THE ANNUAL REPORT FOR THE FINANCIAL YEAR 2016

In accordance with the third paragraph of Article 272 and Article 546. a of the Companies Act (ZGD-1), the Management Board of Banka Intesa Sanpaolo d.d. has prepared and forwarded to the members of the Supervisory Board the following documents for review and approval:

- The Audited Annual Report for the Financial Year 2016,
- The Auditor's Report drawn up by the independent auditor KPMG Slovenija, Limited Liability Company,
- The proposal for the appropriation of profit and
- The report on the relations of the Bank with controlling company and its affiliates including the Auditor's Report drawn up by the independent auditor KPMG Slovenija, Limited Liability Company.

Pursuant to the provisions laid down in Article 282 and Article 546. a of the Companies Act, the Supervisory Board has examined the received documents and hereby presents its findings to the Annual General Meeting of Shareholders of Banka Intesa Sanpaolo d.d. (hereinafter referred to as: AGM) as follows

R E P O R T

1. The way and scope of verification of the management of the Bank during the financial year 2016

In the course of the financial year 2016, the Supervisory Board of the Bank met five times at ordinary meetings and fifteen times at extraordinary meetings in which it
examined:
- strategic and operating matters in relation to the Bank's development,
- implementation of the business policy and current results posted by the Bank,
- annual and other reports of the Management Board, as well as other important issues relevant to the Bank' business;

and voted:
- on proposed business deals where due to being in excess of the limit on exposure determined for a particular customer, the Supervisory Board of the Bank has to grant its prior approval and
- on other matters of interest.

The materials for the meetings were forwarded to the members of the Supervisory Board in compliance with the Rules of Procedures governing the discharging of the functions of the Supervisory Board and those functions were discharged in line with the aforementioned enactment.

In 2016, the composition of the Supervisory Board changed. The 35th AGM held on 27 June 2016 was informed that the term of office of the members of the Supervisory Board: Vojko Čok, Roberto Civalleri, Dr Borut Bratina, Emanuele Collini and Elena Breno expired on 27 June 2016. On the same day Vojko Čok, Dr Borut Bratina, Emanuele Collini, Elena Breno and Silvia Rinaldi were elected. The Supervisory Board elected at its meeting held on 29 June 2016 Vojko Čok as the chairman and Dr Borut Bratina, as the deputy chairman of the Supervisory Board. Since Vojko Čok resigned his position on the Supervisory Board effective 19 December 2016, Uroš Čufer was elected as a new member of the Supervisory Board by the 36th AGM held on 19 December 2016. The Supervisory Board appointed at its meeting held on 20 December 2016 Uroš Čufer as the chairman.

The Supervisory Board performed its duties in accordance with its principal function, i.e. supervision of the Bank's business run by the Management Board and the Bank's performance in accordance with its powers and focused attention to the following areas, in particular:
- gave prior approval to the budget for the financial year 2016;
- monitored and assessed on a regular basis the compliance with the Bank's business policy for 2016 and the fulfilment of the goals set out within the policy framework;

- approved The target values for the NPL ratios for the period 2016 – 2018 and monitored the NPL reduction trends;
- approved the transfer of shares of Visa Europe Limited to Visa Inc.;
- received the Letter issued by the Bank of Slovenia (hereinafter referred to as: BoS) to the Management Board and Supervisory Board after the review of the Payment System MKA and operations performed by the Bank in the role of the operator of the payment system complete with the Bank's plan of activities with regard to the realisation/ fulfilment of BoS' requirements from the Letter; and monitored further steps/activities of the Bank;
- gave consent to the use of the internal credit rating model for Small Business Risk Segment and to the module for economical group influence for Corporate Risk Segment;
- took note of the restructuring guidelines for Micro, Small and Medium-sized Companies issued by the Bank of Slovenia;
- adopted The 2016 recovery plan Intesa Sanpaolo Group, Contribution of Banka Koper, prepared by the Group Intesa Sanpaolo in accordance with the EU Bank Recovery and Resolution Directive (BRRD);
- discussed the annual plan of the Internal Audit Assignments for the year 2016 and the multiyear plan for the period 2016 – 2018;
- examined the annual report on the carrying out of internal control and the measures that arise from the regulations from the field of the fight against money laundering and terrorist financing, and the implementation of restrictive measures for 2015 and the semi-annual for the first half of 2016;
- examined the semi-annual report on the Internal Audit Assignments for the second half of 2015 and for the first half of 2016, examined and approved the annual report of the Internal Audit Department for 2015;
- verified the activities and reviewed the findings of the Internal Audit Department during the current year;
- gave the declaration on the adequacy of the risk management arrangements and the concise risk statement describing the Bank's overall risk profile associated with the business strategy;
- adopted the annex to the Intesa Sanpaolo Group Remuneration Policy;
- proposed to the AGM to elect new members of the Supervisory Board due to the expiry of the term of office of the Supervisory Board and one resignation notice given;
- agreed with the assignments given to the audit firm KPMG for the limited review of the reporting packages for 2016-2017 period;
- took note of the minutes of the Audit Committee, Risk Committee and Nomination Committee meetings;
- gave consent to the sale of the shareholding in the company Intesa Sanpaolo Card, d.o.o., Zagreb, Croatia;
- appointed the new chairman of the Supervisory Board;
- appointed new members of the Audit Committee, Risk Committee and Nomination Committee;
- took note of the new Bank's Compliance Policy;
- examined the ICAAP Book;
- monitored the Bank's capital adequacy;
- gave consent to the write-offs of overdue and unrecoverable Bank's receivables;
- gave consent to the large exposure in relation to the individual clients of group of related parties;
- approved the updates on Intesa Sanpaolo Group Remuneration Policy for 2016;
- proposed to the AGM the modifications of the Articles of Association mainly due to the change of the Bank's name;
- addressed other issues in accordance with powers conferred upon it under law and the Articles of Association.

The Audit Committee, Risk Committee and Nomination Committee provided the Supervisory Board with substantive support in 2016.

The Supervisory Board assesses that it had at its disposal timely and adequate data, reports and information, as well as additional clarifications and explanations when required at sessions it held, so as to be able to monitor throughout the financial year the Bank's operations with due attention, as well as the internal audit function and supervise the running of the Bank. In February 2017 the members of the Supervisory Board examined the extensive report on the performance and the results posted by the Bank in 2016, arising from the audited accounting statements.

The Supervisory Board hereby states that all its members have examined carefully the Annual Report, the Report of the Certified Auditor, Financial Statements, Notes to the Financial Statements, and other notes presented therein. Furthermore, the Supervisory Board assesses that the Annual Report of the Management Board gives a true and fair view of the business events and provide comprehensive information as to operations during the past financial year, and thus complements and expands the information already presented to the Supervisory Board in the course of the financial year. The Bank has safeguarded a high level of operational safety and effectively manages risks it is exposed to in the course of its day-to-day business. Therefore, the Supervisory Board has assessed that considering the circumstances under which the Bank conducted business, the Bank's management and performance were successful during the period under review.

Furthermore, the Supervisory Board also assessed that the work of the Internal Audit Department was well planned and effective, and supported the activities of the Management Board, Audit Committee and assisted the Supervisory Board when forming opinions and making assessments.

2. The position with regard to the Independent Auditor's Report

The Supervisory Board hereby concludes that the external auditor has expressed in the Auditor's Report an opinion in relation to the financial statements prepared by Banka Koper d.d. On this basis, the Supervisory Board hereby adopts the following

p o s i t i o n:

that the Supervisory Board has no objection to the Report of the auditor KPMG Slovenija, limited liability company.

3. Approval of the Annual Report for the financial year 2016

On the basis of the insight into operations carried out by the Bank in the course of the financial year and after due examination of the audited Annual Report and the unqualified opinion stated in the external auditor's report, the Supervisory Board hereby

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The Annual Report of Banka Koper d.d. for the Financial Year 2016.

4. Approval of the proposal on profit appropriation

The members of the Supervisory Board have analysed the proposal regarding the appropriation of the balance-sheet profit. They have found the proposal for the adoption of the distributable profit, to be in line with the dividend policy of the Bank. After due examination of the proposal, the Supervisory Board hereby fully

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with the proposal of the Management Board on the appropriation of the profit.

5. Confirmation of the Report on the relations of the Bank with the controlling company and its affiliates for 2016

5.a. Position with regard to the Auditor's Report

The Supervisory Board hereby establishes that the external auditor in its report has given the following opinion regarding the Report on the relations of the Bank with the controlling company and its affiliates:
»Based on the procedures we have performed and the evidence we have obtained, nothing has come to our attention that causes us to believe that the:

- statements in the report on relations with affiliated companies for the financial year that ended 31 December 2016 are not accurate in all material respects;
- that the Company's execution of legal transactions stated in the Report was disproportionally high in view of circumstances that were known at the time when these transactions were performed;
- that circumstances exist that would in view of other actions mentioned in the Report indicate a significantly different assessment of the disadvantage from the one given by the management, all by taking into account the above-mentioned criteria.«

The Supervisory Board hereby adopts the following

p o s i t i o n:

The Supervisory Board does not have any objection with regard to the Report of the audit firm KPMG Slovenija.

5.b. Statement of the Management Board of the Bank with regard to the Report on the relations of the Bank with the controlling company and its affiliates

The Management Board of Banka Koper d.d. with regard to the Report on the relations of the Bank with the controlling company and its affiliates has stated that Banka Koper d.d. in the circumstances known to it at the time when a legal transaction was carried out or abandoned, the Bank received adequate compensation and by the act of abandonment, it was not to its detriment. The Supervisory Board has no objection with regard to the Statement.

Based on the disclosures and information regarding the Bank's operations during the year under review and in-depth examination of the Report on the relations of the Bank with the controlling company and its affiliates and the unqualified opinion of the independent auditor, the Supervisory Board hereby

c o n f i r m s a n d a p p r o v e s

The Report on the relations of Banka Koper d.d. with the controlling company and its affiliates.

Koper, 16 February 2017

Chairman of the Supervisory Board
Uroš Čufer

3. BODIES OF CORPORATE GOVERNANCE

Supervisory Board

The Supervisory Board of Banka Koper d.d is composed of five members: two independent experts and three representatives of the Intesa Sanpaolo banking group.

In 2016, the composition of the Supervisory Board changed. The 35th Annual General Meeting of Shareholders of Banka Koper d.d. (hereinafter referred to as: the AGM) held on 27 June 2016 was informed that the term of office to the members of the Supervisory Board: Vojko Čok, Roberto Civalleri, Borut Bratina, Ph.D., Emanuele Collini and Elena Breno expired on 27 June 2016. On the same day Vojko Čok, Borut Bratina, Ph.D., Emanuele Collini, Elena Breno and Silvia Rinaldi were elected. The Supervisory Board elected on its meeting held on 29 June 2016 Vojko Čok as the chairman and Borut Bratina, Ph.D. as the deputy chairman of the Supervisory Board. Since Vojko Čok resigned his position of the Supervisory Board effective 19 December 2016, Uroš Čufer was elected as a new member of the Supervisory Board by the 36th AGM held on 19 December 2016. The Supervisory Board elected on its meeting held on 20 December 2016 Uroš Čufer as the chairman.

Members of the Supervisory Board

As at 31 December 2016:	
Uroš Čufer	*Chairman*
Borut Bratina, Ph.D.	*Deputy Chairman*
Elena Breno	*Member*
Emanuelle Collini	*Member*
Silvia Rinaldi	*Member*

At the end of 2016, the Bank had three committees of the Supervisory Board, namely Audit Committee, Risk Committee and Nomination Committee.

Management Board

The Management Board of Banka Koper d.d. has seven members.

In 2016, the term of office of Mr Giancarlo Miranda as the president of the Management Board expired. He was re-appointed by the Supervisory Board on its meeting held on 29 June 2016 for a period of five years.

Members of the Bank's Management Board

As at 31 December 2016:	
Giancarlo Miranda, M.Sc.	*President*
Igor Kragelj	*Deputy President*
Irena Džaković	*Member*
Rado Grdina	*Member*
Aleksander Lozej, M.Sc.	*Member*
Maurizio Marson	*Member*
Aleksander Milostnik	*Member*

4. ECONOMIC AND BANKING ENVIRONMENT

After growing for two years, economic activity in Slovenia continued to grow also in the course of 2016. The exports sector remains successful mostly as a result of increased foreign demand and gains in export competitiveness of Slovenian firms. Last year, the increase in private consumption had a favourable effect on GDP growth with consumption rising in the durable goods segment as well as in other segment. The contribution of government consumption to the growth was also positive. As opposed to rising private investments, the contraction in government investment was rather sharp and mainly attributable to the fall in investment upon the transition to the implementation of the new EU financial perspective.

In line with the favourable trends in economic activity, the labour market situation also improved. At the end of December, 99,615 people were registered as unemployed, which is 11.9% lower than in December 2015. Despite lower unemployment, the structural mismatches in the labour market are rising, which means that companies encounter difficulties when recruiting staff due to the mismatch of labour market needs and skills.

After more than a year and a half of falling prices, annual inflation rose to 0.5% in 2016 (in 2015 it remained negative: -0.5%). As private consumption gained momentum, prices for services went up and contributed the most to price growth, as opposed to oil price hike in the international markets that remained relatively low.

In the course of 2016, there was the improvement in the general government balance year-on-year. Revenues went up primarily due to the more favourable labour market situation. Expenditures were also lower largely due to the fall in general government investment. On the other hand, other lines of expenditure rose with the partial easing of the austerity measures and higher spending on goods and services.

During the year under review, the activities aimed at consolidation and privatisation of the Slovenian banking system continued, even though the positive effects of the favourable economic developments fell short of benefiting bank lending activity. The negative effect of declining lending to corporate customers was only partially neutralised by higher lending to households. On the one hand, banks remain cautious when lending to corporates and on the other companies turn to internal sources of financing their needs and funding obtained by issuing bonds is more frequent. Banks tend to favour financing of households, since the Slovenian households are among the relatively least indebted in the euro area, and their position is improving as the labour market situation is improving. In the course of 2016, all kinds of lending to households enjoyed growth. A gradual recovery of the real estate market and low lending interest rates had a beneficial effect on housing loans. Booming housing loans triggered the rise in consumer loans and eventually of other forms of borrowing. The quality of banks' loans improved further in 2016; banks decreased their non-performing loans by restructuring, write offs and sales of NPLs at a discount.

On the liability side of the balance sheet deposits on the non-banking sector continued to grow in the course of 2016, particularly in the household and corporate segments, as opposed to the deposits of the general government segment. In the low interest rate environment shorter deposit maturities prevailed with sight deposits going up.

The contraction in the lending volume and low interest rates on the asset side of the balance sheet affected the banks' operating results. Interest income in December 2016 stood by almost 20% below the same figure a year earlier even though the negative effect was partly neutralised by the banks' lower interest expense. Operating costs remained relatively stable and the black figures were once again attributable to lower expense for impairments and provisions that plunged in 2016 year-on-year.

5. AN OVERVIEW OF THE BANK'S OPERATIONS IN 2016

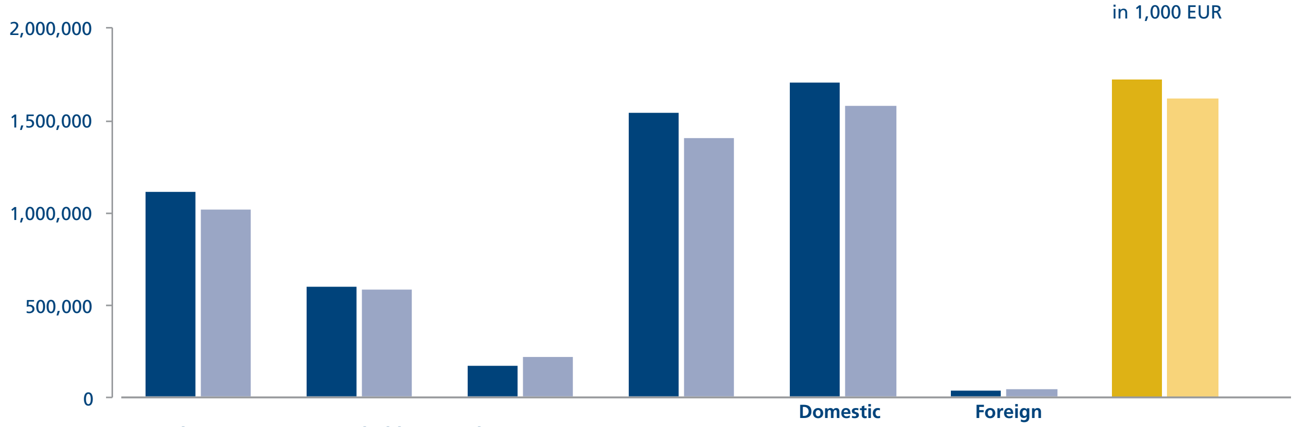
5.1 LENDING OPERATIONS

The recovery of economic activity did not contribute to halting the downward trend of the volume of loans that we have witnessed since 2011, however the decline slowed somewhat. Gross loans at the end of December 2016 amounted to 22.6 billion euros, representing a 3.3 per cent decrease compared to the end of 2015.

In 2016, the Bank's gross lending to the non-banking sector increased by 107.2 million euros, i.e. by 6.6 per cent in comparison with 2015. The Bank's non-banking lending market share increased by 71 b.p. and reached 7.6 per cent at year-end 2016.

In terms of currency, lending in euro still largely prevailed in 2016 with a 98.5 per cent share in total lending activities. As for the maturity structure, the trend of increasing long-term over short-term loans was recorded also in 2016. Short-term loans accounted only for 10.4 per cent of total loans.

An overview of gross lending to the non-banking sector in thousands of euros



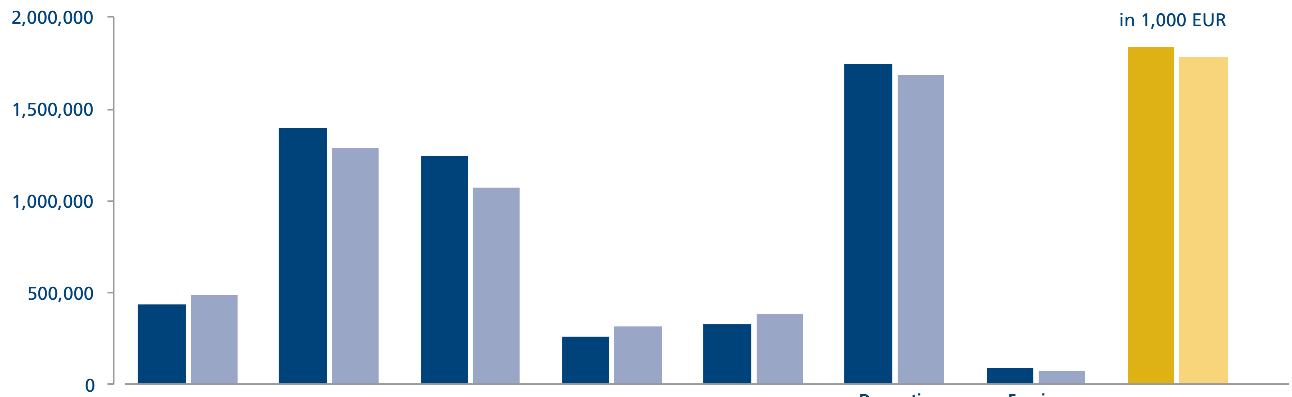
	Legal entities	Households	Short - term	Long - term	Domestic currency	Foreign currency	TOTAL
2016	1,129,647	601,097	179,970	1,550,773	1,704,275	26,470	**1,730,743**
2015	1,041,900	581,664	222,210	1,401,354	1,590,668	32,897	**1,623,564**

Loans to the corporate sector amounted to 1,129.7 million euros or 65.3 per cent, representing the largest portion of loans to the non-banking sector.

Lending to households (private individuals and sole proprietors) reached 601.1 million euros or 34.7 per cent of total lending to the non-banking sector. Compared to 2015, lending to this customer segment increased by 19.4 million euros or 3.3 per cent. As in 2016, households mostly borrowed on a long-term basis, while borrowing in foreign currency remained on a low level. Most of long-term loans are mortgage loans. In 2016, the Bank maintained its market share in the segment of private individuals and sole proprietors, which amounts to 6.6 per cent, while the market share in the segment of corporate clients increased from 7.1 per cent to 8.4 per cent.

5.2 DEPOSITS

An overview of deposits and loans from the non-banking sector in thousands of euros



	Legal entities	Households	Sight	Short - term	Long - term	Domestic currency	Foreign currency	TOTAL
2016	435,412	1,404,552	1,245,521	259,523	334,919	1,751,778	88,185	**1,839,963**
2015	484,206	1,292,539	1,069,311	318,491	388,943	1,689,560	87,185	**1,776,745**

In 2016, the Bank increased deposits and loans from the non-banking sector by 3.6 per cent or 63.2 million euros, while the market share decreased by 3 b.p., to 7.0 per cent; on the contrary, the market share of household deposits increased by 17 b.p. and amounted to 8.2 per cent at the end of 2016.

The sight deposits accounted for a 67.7 per cent share of all deposits followed by long-term deposits (18.2 per cent) and short-term deposits trailing at 14.1 per cent. The deposit structure in terms of currency was dominated by deposits denominated in euro with 91.8 per cent. In 2016 sight deposits increased by 16.5 per cent, while short-term and long-term deposits decreased. Short-term deposits decreased by 18.5 per cent and long-term by 13.9 per cent, compared to the previous year.

The volume of the deposits placed by legal persons increased by 4.4 per cent (by 15.7 million euros) comparing with 2015. Also in 2016, the deposit structure in terms of currency was dominated by deposits denominated in euro.

Household deposits accounted for 76.3 per cent of all non-bank deposits and at the end of 2016 totalled 1,404.6 million euros, i.e. 112.0 million euros more year-on-year. Household deposits were mainly denominated in local currency.

5.3 OTHER SERVICES

5.3.1 Card operations

The Activa System

In 2016, the banks members of the Activa system continued with the issuance of contactless cards and with equipping points of sale with contactless POS terminals. Some banks also introduced a solution for mobile authentication that enables customers a simpler process of confirming identity at secure internet shopping and namely only by using the dedicated mobile application. Digitalisation of operations will be continued in the Activa system also in 2017, and namely by the envisaged use of the mobile wallet that will primarily enable carrying out card mobile payments.
The year under review was also marked by the implementation and adjustment to Chapter II of REGULATION (EU) 2015/751 on interchange fees for card-based payment transactions.

Additionally in 2016 in the Activa system due to the consolidation of the banking system in Slovenia there were certain changes in the status of the banks members of the Activa system (Banka Celje was merged into Abanka and PBS was merged into NKBM).

Banka Koper

In the beginning of 2016, Banka Koper enabled on its own AZM the acceptance of the cards of the company UnionPay International, which is the largest issuer of payment cards in the world.

In mid-2016, Banka Koper based on the obtained authorisation for the issuance of the payment debit and credit cards in Great Britain started with the issuance of the latter to the customers of the bank Intesa Sanpaolo Private Banking, London Branch.

In 2016, Banka Koper after successfully completing the pilot phase as the first bank in Slovenia, achieved by commercial launching of the mobile wallet Wave2Pay an important milestone in the introduction of mobile card payments. Mobile card payments function on the basis of the HCE technology (Host Card Emulation), where payment credentials where needed are transferred from the Cloud to the phone for smooth execution of payments. At present, it is possible to make mobile payments with the product Activa Mastercard, in the next year Banka Koper will offer that opportunity also for other card products.

Banka Koper confirmed its orientation to the digital area in 2016 also by introducing the prepaid QL account, which enables non-customers of Banka Koper to apply online and execute QL payments on the points of sale enabled for it and QL transfers to other QL users within the framework of pre-loaded funds on QL account. QL payments, i.e. transfers enable the users to execute transactions by means of mobile devices with immediate availability of the paid, i.e. transferred funds.

In 2016, the promotion of launching the mobile wallet Wave2Pay and introduction of mobile card payments were at the forefront. At the same time, Banka Koper promoted in 2016 the use of the card products Activa MasterCard, Activa Visa and American Express. To the users of those cards Banka Koper offered and with it enabled a series of benefits on points of sale.

New products and services

Banka Koper in 2016 broadened to its customers the offer of products and services on the basis of their expectations, market conditions and legislative requirements. Of all of them, it is worth highlighting the following:

- Shema ugodnosti Moj Paket;
- Shema »Zaupaj mi, jaz ji zaupam« where Banka Koper rewards its loyal customers who recommend Banka Koper to new customers;
- The offer of insurance products connected to accident insurance, additional health insurance, tourist travel insurance, automotive insurance, non-life insurance and life assurance;
- Combination of savings in investment funds and long-term deposit;
- Pre-approved consumer credits;
- Mobile wallet Wave2Pay with the following functions: mobile payment, mobile authentication, push notification (get a notification for transactions) and transactions review;
- The prepaid QL account, which enables non-customers of the bank to apply online and execute QL payments on points of sale enabled for it and QL transfers to other QL users within the framework of pre-loaded funds on QL account;
- Iz(i)voz – insurance and financing exporters;
- Benefits for newly established companies and societies.

5.3.2 Marketing and sale of mutual investment funds

In 2016, the falling trend in interest rates on deposits continued, but due to frequent fluctuations on capital markets, investors showed no signs of particular optimism. In the Slovenian funds more funds were paid out in 2016 than paid in. Despite that, the funds in the Slovenian funds increased in that period. Mutual funds of foreign management companies (DZUs) were faced with funds outflows according to the data of Bank of Slovenia.

Against the backdrop described above, Banka Koper may be proud of its good performance, since in 2016 it realised 2 million euros in net sales. Consequently, the market share of Banka Koper in terms of funds in foreign funds on the Slovenian market increased and exceeded 23%.

The selection of the foreign funds marketed by Banka Koper increased in 2016 by five new mutual funds – four flexible funds of the fund of funds Eurizon EasyFund (Absolute Prudente, Bond Flexible, Flexible Multistrategy and Azioni Strategia Flessibile) and one new fund dedicated exclusively to legal entities (Eurizon EasyFund Treasury EUR T1). Thus at present the offer is composed of the folloowing funds:

- Eurizon Capital WITH. A. (26 mutual funds Eurizon EasyFund and four mutual funds Eurizon Manager Selection Fund),
- Franklin Templeton Investments S. A. (10 mutual funds Franklin Templeton Investment Funds).

In addition, Banka Koper marketed also the funds of three Slovenian management companies:

- ALTA Funds – 23 funds,
- KBM Infond – 25 funds,
- Primorski skladi – 4 funds.

In 2015, Banka Koper started with the project MiFID II and Wealth Management. The purpose of the project is to set up an advisory model, which is aligned with the MiFID II and the strategy of the Group ISP. In order to be able to provide investment advising, both the bank and its employees working in that area must obtain appropriate licence. To that end Banka Koper submitted in June 2016 the application to Bank of Slovenia and to the Securities Market Agency (ATVP) for obtaining the licence for investment advising. On 27 December 2016 Banka Koper received the licence for providing investment advising and investment research and financial analyses relating to transactions with financial instruments.

In addition, as many as 21 employed successfully passed the broker examination and obtained the authorisation for investment advising.

The good performance was possible to achieve also thanks to the marketing campaigns with which Banka Koper lowered to investors the entry fees and the strengthened marketing of savings schemes in mutual funds. Consequently, in 2016, 522 new savings schemes were concluded, which was a record high since Banka Koper started marketing mutual funds.

For the sixth year in a row, the journal Moje finance scored the quality of the mutual funds marketed in Banka Koper. According to the selection of the journal Moje finance, the foreign mutual funds, which are marketed in Slovenia by Banka Koper, won five awards for the best funds; in addition to the aforementioned awards the expert jury awarded five stars to two more mutual funds for quality.

5.3.3 Leasing

Finor Leasing Office, which is an integral part of the business network in the area of operations with small and medium-sized enterprises, is specialised for selling financial leasing across the territory of Slovenia, both for natural persons and legal entities.

At Finor Leasing Office there are eight employees who work in three units in Koper, Ljubljana and Maribor. In 2016, 427 leasing contracts were concluded in the total amount of 13.7 million euros. Most contracts – 210 of them in the amount of 7.5 million euros – were concluded for commercial vehicles, followed by personal vehicles with 643 contracts in the amount of 3.7 million euros, production and other equipment with 33 contracts in the amount of 1.7 million euros, real estate with 4 contracts in the amount of 0.7 million euros, and yachts with 3 contracts for the amount of 0.2 million euros.

5.3.4 Open-ended mutual pension funds (OVPS) of Banka Koper

Banka Koper d.d. is actively included in the voluntary supplementary Slovenian pension insurance system, since already back in 2001 it established and started managing the Open-ended mutual pension fund of Banka Koper d.d. – OVPS. The latter is both for collective and individual additional pension insurance.

As at 31 December 2016, the total assets of the pension fund of Banka Koper – OVPS had the total amount of 40.798 million euros, which is a 10.65% increase in comparison with the end of 2015. The increase is mainly a consequence of the merger of the pension fund of Abanka d.d. – AIII to the OVPS pension fund and a significant decrease in the pressure of the insured persons for paying out the saved funds in a single amount.

Despite the fact that the tax treatment of an extraordinary exit from the second pillar is prohibitive in comparison with an ordinary exit, it is worth underlining that when it comes to pay outs, extraordinary exits (one-off payment) from the second pillar still prevail in comparison with ordinary exists (additional pension benefit). Nevertheless, in 2016 there was a clear positive trend in using the saved funds in the form of additional pension – a rent.

In the OVPS pension fund at the end of 2016 there were 7,317 insured persons, which is approximately the same number as a year earlier. Of that number 6,793 insured persons were included in collective voluntary additional pension insurance, 635 in individual insurance. There were 108 companies that co-finance collective pension schemes in the OVPS.

The net asset value per share – NAV of the OVPS pension fund as at 31 December 2016 was 9.6261 euros and it increased by 2.04% year-on-year, which is above the guaranteed yield that in 2016 was 1.075%. The five-year yield of the OVPS pension fund as at 31 December 2016 was 17.25%, whereas the VEP growth since the establishment of the OVPS pension fund until 31 December 2016 is 130.84%.

Banka Koper d.d. decided in 2016 to continue to offer to its insured persons the mutual pension fund with the guaranteed paid net premium and the guaranteed minimum yield. In 2016, Banka Koper d.d. also adopted a decision with which it decided to transform the pension fund, which offers the guaranteed yield, to a fund of pension funds with three sub-funds whose investment policy, whose investment policy would be adjusted to different age structure of its insured persons, the so-called life cycle investment policy.

The life cycle investment policy is the expanded method of the investment strategy around developed economies where the savings horizon is long and intended for acquiring additional assets for the purpose of paying out additional pension once the insured person retires. Such a form of the investment policy offers to younger population of insured persons more risky investment oriented into shares, whereas as the insured person gets older and approaches the age for retirement, the level of risk gradually decreases down to the last, lowest level of risk, when the insured persons are again part of the guaranteed pension sub-fund and are the members of that sub-fund until the selection of the payer of the additional pension; hence until retirement.

5.3.5 Depositary banking

Banka Koper d.d. was the first bank in Slovenia to provide depositary services for investment funds back in 2004. It has acquired enormous knowledge and experience in that area since then. The provision of depositary service calls for daily control of the correctness of the items in the books of account of the funds, checking and verifying the correctness of the calculation of the net amount of assets and the value of net asset value per unit, examining conversions of payments made and requests for pay outs, as well as of the compliance of investments with the provisions of the investment policy. Depositary is also custodian of the assets of each investment fund, since the latter is kept on the accounts opened by depositary in the name and for the account of an individual fund – the final beneficiary. Depositary is custodian of the correctness of the operations of the investment fund, as well as of its assets.

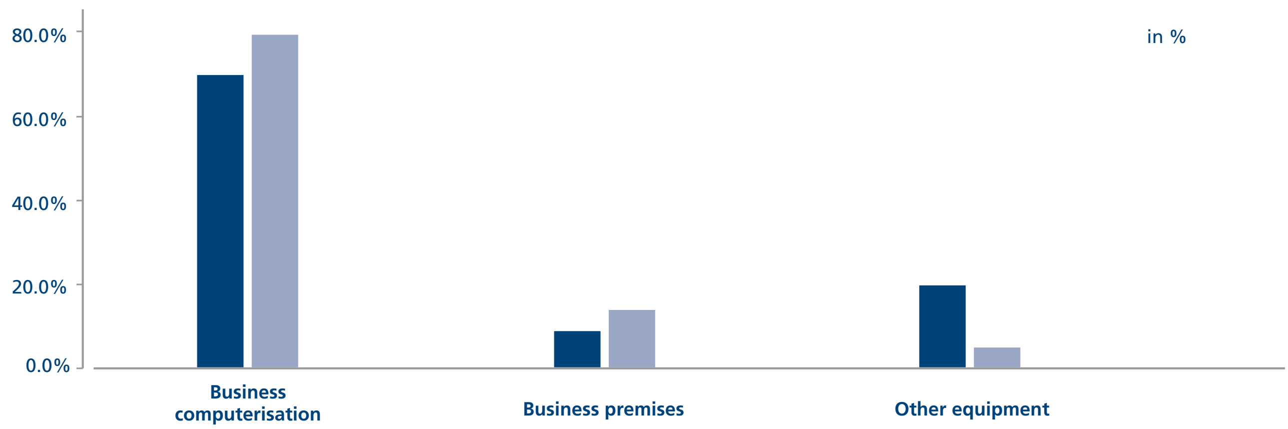
At the end of 2016, Banka Koper d.d. was providing depositary services for 45 mutual funds, for 5 pension funds and 5 internal funds at insurance undertakings. The volume of assets in custody exceeded 1.1 billion euros.

6. THE BANK'S ORGANIC GROWTH AND DEVELOPMENT

6.1 CAPITAL INVESTMENTS

Banka Koper continued in 2016 its long-term development programme and invested 1.2 million euros in the computerisation of business, commercial premises, and other equipment. However, the Bank allocated 0.8 million euros less to investments than in the previous year.

Structure of capital investments in 2016



	Business computerisation	Business premises	Other equipment
2016	71,1%	8,5%	20,5%
2015	80,9%	14,2%	4,9%

The majority of investments, 0.9 million euros or 71.1 per cent were allocated to the computerisation of business. Increasingly stricter requirements regarding banking safety demand yearly investments in ensuring the safety of services.

In 2016, the Bank assigned a total of 0.1 million euros or 8.0 per cent of all investments to the conversion of its commercial premises into a modern banking service and to the design of its branches according to the corporate identity of the banking group.

6.2 INFORMATION TECHNOLOGY AND TECHNOLOGICAL DEVELOPMENT

In the area **of business solutions,** Banka Koper in 2016:

- Continued with the implementation of the solutions **Mobile payments (QL).** It is about Banka IN **»mobile wallet«**, an innovative the solution on the Slovenian market. The solution complements the existing payment mechanisms, replaces cash operations and payments of small amounts and enables to perform domestic payment transactions in a simple and transparent way both for the provider of service and the user in real time. The solution is designed for customers and non-customers of Banka Koper;
- started with activities on project within the framework of the Group IntesaSanpaolo, **»Global Transaction Banking«**, and namely under the implementation of »Cash management« and efficient carrying out of cross-border payments, while in the Slovenian environment it started with the intensive preparations for carrying out payment transactions in real time;
- started with the preparation of rules, procedures and setting up of the technological support **»Wealth Shaper«** for carrying out the processes of **investment advising** in accordance with the provisions of **Mifid** and it obtained the authorisation for the provision of the investment service – investment advising and investment research and financial analyses related to operations with financial instruments. The process of investment advising comprises the determination of the investor's profile, the analysis of the current portfolio, the presentation of the recommended portfolio, the preparation of an offer, executing orders and after-sale activities. Banka Koper will introduce the processes of investment advising and the use of the technological support »Wealth Shaper«in the course of 2017;
- set up the procedures and started with marketing of the new **fund Eurizon**.

In the area of risk management Banka Koper in 2016:

- introduced in accordance with the guidelines the parent bank a technological solution for **the calculation of provisions and classification** of customers for the needs of reporting;
- introduced in accordance with the guidelines the parent bank a single technological support for **proactive management, monitoring and early detection of increasing risk level** of the customers who are legal entities;
- Introduced technological support for the management, keeping and monitoring the cases in the **hard debt collection** procedures. The hard debt collection procedures are thus more efficient and transparent as processes;
- continued with activities in the area of the optimisation of credit processes and in accordance with the guidelines the parent bank upgraded the technological **support for legal entities credit process** and set up the exchange of data with the parent bank.

In the **regulatory** area and the compliance area Banka Koper in 2016:

- upgraded the technological solution for **interest-rate risk management** with the functionalities for determining availability of the market interest rate within the transfer price of financing (FTP) and negative interest rates management with the aim to meet regulatory requirements of the central bank and the parent bank;
- renewed the reports to Banka Slovenije in accordance with the regulations of the central bank (the credit register);
- in accordance with the requirements of the parent bank amended reporting on the credit portfolio and prepared other reports for the purpose of monitoring operations;
- in accordance with the Deposit Guarantee Scheme Act put in place internal procedures and renewed reporting for the central bank;
- in accordance with the guidelines of the parent bank put in place the project **»The system for data management«** whose objective is to out in place internal rules, procedures and organisation for data management, upgrading the existing solutions and the data warehouse, and the establishment of a central base data within the framework of the parent bank. The implementation of the first phase of the project is planned to take place in 2017;
- continued with the project **Internal controls** with the aim of more efficient control and management of the banking processes. New business processes and technological solutions for managing controls in credit processes were introduced.

In the area of the **optimisation of operations** Banka Koper in 2016:

- started with the project for the overhaul of the **ERP system for the cost accounting management and fixed assets cost accounting**. Once the project implementation is completed in March 2017, Banka Koper will optimise its technical infrastructure, internal processes and introduce paperless operations also in that area;
- continued with the modernisation of the **equipment for a teller's/cashier's workplace** where after the equipment for electronic signing of documents in 2013 also the equipment for electronic capturing of the documentation on site of its generation was introduced. With it Banka Koper will have in place completely paperless functioning of a teller's/cashier's workplace, it will optimise its business processes, speed up the most frequent operations, and significantly reduce the costs associated with archiving documentation;

In the area of **information security**, Banka Koper in 2016:

- in the area of the card-based operations **implemented the protection of sensitive data (Primary Account Number - PAN)** with the »tokenization« method;
- in accordance with the ECB guidelines in the area of internet-based payments, Banka Koper **implemented the solution for the detection of abuses in the internet-based and mobile banking**. In 2017, Banka Koper is planning to set up a process of regular monitoring of abuses in that area. The solution can be upgraded also in other areas of banking operations;
- continued with the optimisation and centralisation of the **banking information infrastructure** and started with the work on the data centre in Slovenia in accordance with the BCM guidelines of the parent bank.

In the area of **energy efficiency**, Banka Koper carried out a partial energy renovation of the central building in Koper. The renovation will be continued in the course of 2017.

7. ACTIVITIES IN THE FIELD OF SUSTAINABLE DEVELOPMENT OF BANKA KOPER IN 2016

After the assessment conducted by Bureau Veritas Slovenija in 2015 of the fulfilment of the Ethical Code of the banking group Intesa Sanpaolo adhered to by Banka Koper in the course of its daily business, and based on the results of the assessment, Banka Koper started with the actual implementation of the action plan for improvements. Of all the stakeholders it paid particular attention to setting up an efficient system to ensure and promote safety and health at work; therefore, it participated in the pilot project of the parent banking group in which another assessment, that is, analysis of the gap in the safety and health rights area. The main objective of the analysis was to identify all those non-compliant areas to which Banka Koper must focus attention so that in the years to come it will ensure to the employees the conditions so that with their care they contribute to preserving emotional and bodily health which are of key importance for achieving long-term efficiency at work.

At the same time Banka Koper was carrying out numerous other current activities for preserving and encouraging long-term relationships with all key stakeholders.

7.1 RESPONSIBILITY TOWARDS EMPLOYEES

7.1.1 Training programmes

Systematic training is the foundation of employee development at Banka Koper. The share of funds allocated to education and training in the year under review was 1.18% of administrative expenses of Banka Koper (excluding labour costs). The number of education and training hours totalled 20,518 hours or 27.2 hours per employee. As much as 90% of all education/training was performed in-house by engaging internal and external lecturers/trainers. The Bank's employees delivered 39% of all education and training in 2016.

Since the model designed to provide advice in the area investment services, Banka Koper focused effort on training the employees in the area of investment counselling/advising.

Providing smooth and safe operations also in 2016 called for on-going effort to make all the Bank's employees aware of the significance of the prevention of money laundering and financing terrorism and compliance of all operations carried out by Banka Koper, particularly in the area of personal data protection.

7.1.2 Development of key personnel

In the area of key personnel development, the education and training activities continued within the framework of two programmes: the Talent management project for the development of young employees with high potential and high working performance, and the Project for the development of management staff for manager development that encompasses the development of leaders. Within the framework of both programmes the young employees and managers took part in the workshop with efficient handling stress and effective managing personal energy as the topics. In addition, the young talented employees attended training focusing on assuming responsibility and public professional appearance. At the end of 2016, Banka Koper awarded to the second generation of young talents at the end of the workshop the certificates attesting that they completed a four-year development–training programme.

7.1.3 Concern for and dialogue with employees

In November 2016, throughout the Intesa Sanpaolo Group yet another survey of the organisational climate and employee satisfaction took place. Based on the results of the survey, Banka Koper will prepare a new, that is, updated action plan for the improvement of the areas that will get the lowest scores. Thus to the permanent activities for improving relationships at Banka Koper where necessary new activities will be added which through the employee satisfaction will contribute also maintaining good relationships with our customers.

7.2 RESPONSIBILITY TOWARDS CUSTOMERS

Under the brand name »Posluh 100%«Banka Koper has been carrying out over the past years various activities for the improvement of satisfaction of its customers. These activities include also customer satisfaction research that together with complaints and proposals that customers may submit through various bank's communication channels, present a basis for improving the quality of bank services and relationships with customers. In the first half of 2016, a market survey of customer satisfaction was conducted - Customer Satisfaction Retail Benchmarking Survey, oriented to the customers of our bank and competitor banks in the retail segment and in the corporate segment. Based on 915 expressed opinions, Banka Koper achieved among all banks the highest index of customer satisfaction (ECSI – European Customer Satisfaction Index). The bank scored top marks in the after sales activities, reputation, organisation of its branches and user experiences with the web-based and mobile banking, followed by relationship with customers and cost and quality relation of the bank's products and services.

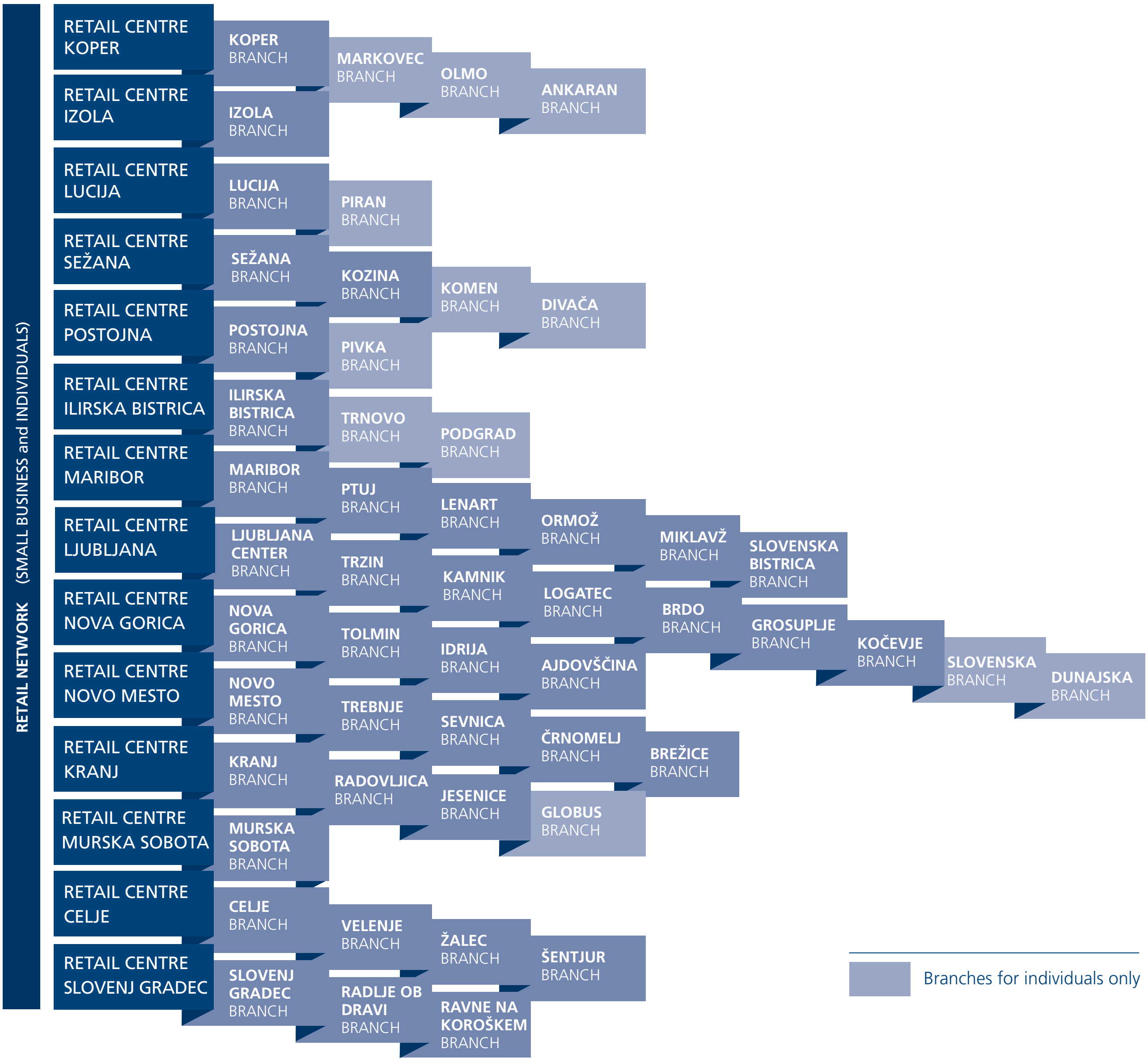
Banka Koper encourages its existing customers to spread the word about the quality of business and the reputation of Banka Koper among their friends and acquaintances within the framework of the motivation programme »Povabi prijatelja« ("Invite a Friend").

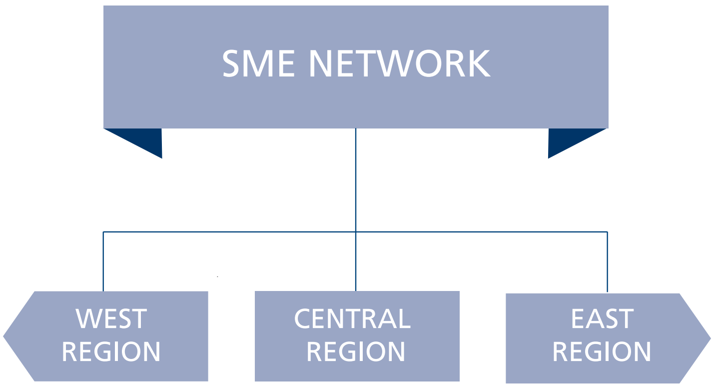
7.3 CORPORATE SOCIAL RESPONSIBILITY

Banka Koper also in 2016 assumed general sponsorship of the second biggest running event in the country and certainly one of major events in Slovenian Istria – the 3rd Istrian Marathon. Running is a sport that brings together an ever increasing number of people of different ages and is evolving into a general movement for a healthy lifestyle and maintaining physical stamina. The positive components of that project, as well as the fact that most participants of the marathon come from other parts of Slovenija in which Banka Koper is present with its branches, is for Banka Koper a sufficient reason for active participation in the project. On the invitation of Banka Koper and the initiative of its parent - the Intesa Sanpaolo Group, the marathon attracted some 200 employees from various European countries. Two former Olympic champions on 10 km and 42 km - Alberto Cova and Gelindo Bordin also accepted the invitation and their participation was a boon to the entire event. Banka Koper used the event to strengthen the relationships among the employees and to that end it invited some 100 employees of Banka Koper to take part in the event.

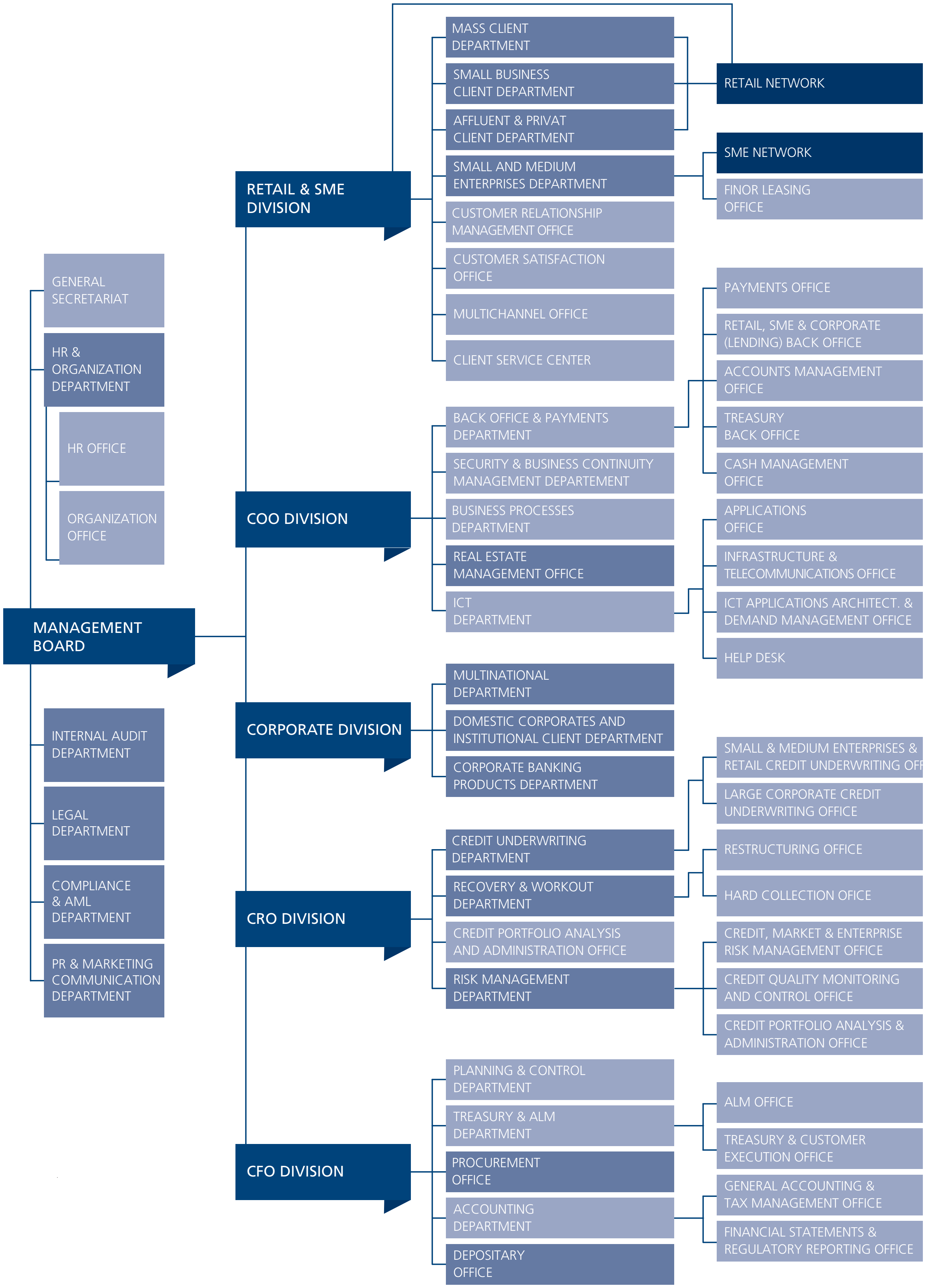
Banka Koper was active although to a lesser degree also in the cultural area, and specifically by supporting in line with the tradition the cultural events in Avditorij Portorož and numerous smaller ones within the framework of the cultural associations.

8. TERRITORIAL CHART OF COMMERCIAL UNITS OF BANKA KOPER D.D.





9. INTERNAL ORGANISATION CHART



10. THE CORPORATE GOVERNANCE STATEMENT OF BANKA KOPER D.D.

THE CORPORATE GOVERNANCE STATEMENT OF BANKA KOPER D.D.

In accordance with the fifth paragraph of Article 70 the Companies Act – ZGD-1 (Official Gazette of the Republic of Slovenia, No. 55/2015), Banka Koper d, d, gives the following

Corporate governance statement
The corporate governance statement is an integral part of the annual report for 2016 and it is available on the website of the company http://www.intesasanpaolobank.si/.

1. The corporate governance code which Banka Koper d.d. decided to use

Banka Koper d.d. hereby declares that for governance it observes the effective legislation, regulations, other legislative and secondary legislative acts and internal rules and instructions.

The company has the two-tier system of governance under which the company is run by the management board; its operations are supervised by the supervisory board. The bodies of the company are the general meeting of shareholders, the supervisory board and the management board.

2. Deviations from corporate governance codes

Banka Koper d. d. for governance does not deviate from the regulations stated in the first point of this corporate governance statement. Banka Koper d.d. does not use any special corporate governance codes, since in that segment it is bound by the codes of the parent bank. Of very high importance for its operations also with regard to governance of the company are the following internal acts:
- Code of Ethics of Banka Intesa Sanpaolo d.d. http://www.intesasanpaolobank.si/
- Code of Conduct in Banka Intesa Sanpaolo d.d

3. The description of the principal characteristics of internal control and corporate governance systems in the company in connection with the financial reporting procedure.

With the aim of ensuring appropriate financial reporting procedures Banka Koper d.d. pursues the Rules of procedure on accounting and accounting policies of the group. Accounting control in the broader sense is provided through the system of internal controls. It shall encompass adequate and effective internal controls, its implementation and monitoring. Internal controls system covers all significant risks to which the bank is exposed and includes checking of administrative and accounting procedures, verification of bank´ s compliance with applicable legislation, standards, codes and internal rules and verification of information security. The descriptions of business processes including control activities for mayor areas of bank´ s business, namely landing, accepting deposits, current accounts and trading business are laid down. The processes related to financial reporting or composition of financial statements (daily and monthly closing of the general ledger) are also set out.

The principal identified risks in this area are managed with an appropriate system of authorisations, delimitation of duties, compliance with the accounting rules, documenting of all business events, the custody system, posting on the day of a business event, inbuilt control mechanisms in source applications and archiving pursuant to the laws and internal regulations. With an efficient controlling mechanism in the area of accounting reporting, the bank ensures:
- a reliable decision-making and operational support system,
- accurate, complete and timely accounting data and the resulting accounting and other reports of the Bank, and
- compliance with legal and other requirements.

In compliance with the Banking Act (ZBan-2) the independent Internal Audit Department is established. The Internal Audit Department performs the tasks of internal auditing and reports on its proceedings to the corporate bodies of the bank.
Risk management at is implemented in accordance with the banking legislation, guidelines of the parent bank and internal policies and procedures in which are laid down the principles and guidance of risk management.

The master business strategy, accepted principles of the bank´ s propensity to assume risk which include the monitoring of risk profile and of specific risks, internal policies of risk management, approved by the bank´ s Management Board and Supervisory Board lay down the objectives and the guidelines concerning the taking of risk and the methods and criteria of risk management.

4. The data on principal shareholders

The data on major direct and indirect ownership of the securities issued by Banka Koper d.d. within the meaning of achieving qualifying holding as specified in the Takeover Act.

The ownership structure of Banka Koper d.d.

Delež kapitalu banke

Naziv	31. 12. 2016	31. 12. 2015
Intesa Sanpaolo S. P. A.	98.,9%	98,4%

5. The data on the holders of securities that give special controlling rights

As at 31.12.2016, no security issued by Banka Koper d.d. gives any special controlling rights.

6. The data on restrictions on voting rights

In relation to the shares issued by Banka Koper d.d., as at 31.12.2016, there are no restrictions on voting rights.

7. Information on the appointment or replacement of members of the management or supervisory bodies and amendments to articles of association

In accordance with the provisions laid down in the articles of association of Banka Koper d.d., in the text in force as of 31.12.2016, the members of the supervisory board are elected by simple majority and discharged by the general meeting of shareholders with a two-thirds vote of the represented share capital. The management board is appointed and dismissed by the supervisory board with simple majority of votes. The general meeting of shareholders decides on amendments to the articles of association with a two-thirds vote of the represented share capital.

8. Information on authorisations to the members of management

The members of management do not have any special authorisations.

9. Information on the general meeting of shareholders of Banka Koper d.d.

In accordance with the provisions of the Companies Act (ZGD-1), the general meeting of shareholders is the ultimate body of the company. The shareholders exercise their management rights in matters of the company at the general meeting of shareholders of the company, where they pass fundamental and statutory resolutions. Convening the general meeting of shareholders is regulated by the articles of association of the company in accordance with effective legislation. The general meeting of shareholders is convened by the management board on its own initiative, at the request of the supervisory board or at the request of the shareholders of the company that represent at least 5% of the share capital of the company. The management board convenes the general meeting of shareholders of the company no less than one month before the meeting. The right to attend the general meeting of shareholders of the company is granted to all the shareholders registered in the shareholder's register as shareholders of the company at the end of the fourth day prior to the general meeting of shareholders, as well as to their proxies and authorised persons, and who apply to the company to attend the meeting no later than at the end of the fourth day prior to the general meeting of shareholders.

At the general meeting of shareholders of Banka Koper d.d. held on 23.06.2016, the shareholders were notified of the annual report of the company for the financial year 2015, the opinion of the independent auditor to the annual report, the report of the supervisory board to the annual report and remuneration of the members of the management board and of the supervisory board in 2015. The shareholders passed the resolution on the distribution the accumulated profit and gave discharge to the management board and to the supervisory board. At the general meeting of shareholders of Banka Koper d.d. held on 19.12.2016, the resolution was passed to change the name of the bank and amend the bank's articles of association.

10. The data on the composition and functioning of the management or supervisory bodies and their committees

The supervisory board

The supervisory board of Banka Koper d.d is composed of five members of which two are external experts and three are the representatives of the Intesa Sanpaolo banking group.

In 2016, there were changes in the composition of the supervisory board. The general meeting of shareholders of Banka Koper d.d. (hereinafter; the general meeting of shareholders) received at its 35th meeting that the term of office of the following members of the supervisory board expired on 27. 6. 2016: Vojko Čok, Roberto Civalleri, dr. Borut Bratina, Emanuele Collini and Elena Breno. On the same day Vojko Čok, dr. Borut Bratina, Emanuele Collini, Elena Breno and Silvia Rinaldi were elected as the members of the supervisory board. The supervisory board appointed on 29. 6. 2016 Vojko Čok as chairman and dr. Borut Bratinao as deputy chairman of the supervisory board. Since Vojko Čok handed in his notice of resignation from the office of member of the supervisory board effective on 19.12.2016, the general meeting of shareholders elected at its 36th meeting held on 19. 12. 2016 a new member of the supervisory board Mr. Uroš Čufer. The supervisory board appointed Uroš Čufer on 20.12.2016 as chairman of the board.

The members of the supervisory board as of 31.12. 2016 so:

Uroš Čufer	chairman
Dr. Borut Bratina	deputy chairman
Elena Breno	member
Emanuele Collini	member
Silvia Rinaldi	member

There were three committees of the supervisory board at the bank at the end of 201: the audit committee, the risk committee and the nomination committee.

The management board

The management board of Banka Koper d. d has seven members.

In 2016, the term of office of Mr. Giancarlo Miranda in the capacity of the president of the management board expired. The supervisory board re-appointed Mr. Miranda as the president of the management board on 29.6.2016 for the period of five years.

The members of the management board as of 31.12.2016 are:

Giancarlo Miranda, M.Sc.	president
Igor Kragelj	deputy president
Irena Džaković	member
Rado Grdina	member
Mag. Aleksander Lozej	member
Maurizio Marson	member
Aleksander Milostnik	member

The corporate governance statement shall be published as a separate report accessible to the general public on the bank's website.

Koper, 14.02.2017

Supervisory board of Banka Sanpolo d. d. Management board of Banka Intesa Sanpoalo d. d.

Financial Report 2016

Independent auditors' report on financial statements

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Independent Auditors' Report

To the owners of the Banka Intesa Sanpaolo d.d.

Opinion

We have audited the financial statements of the Banka Koper d.d. ("the Company"), which comprise the statement of financial position as of 31 December 2016, the statement of profit or loss, statement of comprehensive income, the statement of cash flows, and the statement of changes in equity for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements give true and fair view of the financial position of the Company as at 31 December 2016, and of its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union ("IFRS as adopted by the EU").

Basis for Opinion

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

Other Information

Management is responsible for other information. The other information comprises the Business Report included in the Annual report, but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not apply to other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information; we are required to report that fact. We have nothing to report in this regard.

With respect to the Business Report, we considered whether the Business Report includes the disclosures required by the Company's Act (hereafter referred to as "the applicable legal requirements").

Based solely on the work required to be undertaken in the course of the audit of the financial statements and the procedures above, in our opinion:

- the information given in the Business Report for the financial year for which the financial statements are prepared, is consistent with the financial statements; and

- the Business Report has been prepared in accordance with the applicable legal requirements.

In addition, in light of the knowledge and understanding of the Company and its environment in which it operates, obtained in the course of our audit, we are required to report if we have identified material misstatements in the Business Report and other information that we obtained prior to the date of this auditors' report. We have nothing to report in this respect.

Responsibility of Management and Supervisory Board for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the IFRS as adopted by the EU, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

The Supervisory Board is responsible for overseeing the Company's financial reporting process.

Auditor's Responsibility for the Audit of Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists,

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we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

On behalf of the auditing company

KPMG SLOVENIJA,
podjetje za revidiranje, d.o.o.

Dejan Kurat
Certified auditor

Barbara Kunc
Certified auditor
Partner

KPMG Slovenija, d.o.o.
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Ljubljana, 14th February 2017

The Independent Auditor's Report hereof is a translation of the original Independent Auditor's Report in Slovene, issued on the financial statements and the notes thereto in Slovene and is not to be signed. This translation is provided for reference purposes only.

Statement Of Management's Responsibilities

The management is responsible for preparing financial statements for each financial year that present fairly the state of affairs of the Bank as at the end of the financial year and of the profit or loss for that period.

The management confirms that suitable accounting policies have been used and applied consistently and reasonable and prudent judgments and estimates have been made in the preparation of the financial statements for the year ended 31 December 2016. The management also confirms that the financial statements have been prepared on the going concern basis and in accordance with the applicable laws and International Financial Reporting Standards, as adopted by the EU.

The management is responsible for keeping proper accounting records, for taking reasonable steps to safeguard the assets of the Bank and its subsidiaries and to prevent and detect fraud and other irregularities.

In accordance with local regulations, the tax authorities may at any time inspect the Bank's books and records within 5 years subsequent to the reported tax year and may impose additional tax assessments and penalties. The Bank's management is not aware of any circumstances, which may give rise to a potential material liability in this respect.

Koper, 13 February 2017

President
Giancarlo Miranda

Deputy President
Igor Kragelj

Member
Aleksander Milostnik

Member
Aleksander Lozej

Member
Rado Grdina

Member
Irena Džaković

Member
Maurizio Marson

Financial Statements

1. INCOME STATEMENT

(in thousands of euros)

	Notes	As at 31 December	
		2016	2015
Interest income	4	49,554	56,399
Interest expenses	4	(8,026)	(12,293)
Net interest income		**41,528**	**44,106**
Dividend income	5	655	545
Fee and commission income	6	37,658	40,278
Fee and commission expenses	6	(11,860)	(13,815)
Net fee and commission income		**25,798**	**26,463**
Realised gains or losses on financial assets and liabilities not measured at fair value through profit or loss	7	19,574	2,598
Gains or losses on financial assets and liabilities held for trading	8	812	1,041
Gains or losses on financial assets and liabilities designated at fair value through profit or loss		(48)	71
Fair value adjustments in hedge accounting	9	136	(92)
Exchange differences		(304)	(100)
Gains or losses on derecognition of assets	10	1,043	47
Other operating net income	11	(177)	1,561
Administrative expenses	12	(40,250)	(40,550)
Depreciation and amortisation	13	(4,692)	(5,422)
Provisions and post-employment benefit obligations:		1,123	(243)
- provisions for liabilities and charges	14	1,558	172
- provisions for post-employment benefit obligations and similar obligations	14	(435)	(415)
Impairment	15	(22,239)	(15,827)
Total profit or loss before tax from continuing operations		**22,959**	**14,198**
Tax expense (income) related to profit or loss from continuing operations	16	(2,719)	(2,355)
Total profit or loss after tax from continuing operations		20,240	11,843
Net profit or loss for the financial year		**20,240**	**11,843**
Basic earnings per share (basic and diluted) (in EUR per share)	17	38.16	22.33

The accompanying notes on pages 42 to 101 are an integral part of the financial statements.

2. STATEMENT OF COMPREHENSIVE INCOME

(in thousands of euros)

	As at 31 December	
	2016	2015
NET PROFIT OR LOSS FOR THE FINANCIAL YEAR AFTER TAX	**20,240**	**11,843**
OTHER COMPREHENSIVE INCOME AFTER TAX	**(4,592)**	**(1,880)**
ITEMS THAT WILL NOT BE RECLASSIFIED TO PROFIT OR LOSS	**78**	**(638)**
Actuarial gains (losses) on defined benefit pensions plans	78	(697)
Income tax relating to items that will not be reclassified	-	59
ITEMS THAT MAY BE RECLASSIFIED SUBSEQUENTLY TO PROFIT OR LOSS	**(4,670)**	**(1,242)**
Available-for-sale financial assets	**(5,436)**	**(1,496)**
- revaluation gains (losses) taken to equity	370	2,660
- transferred to profit or loss	(5,806)	(4,156)
Income tax relating to items that may be reclassified to profit or (-) loss	766	254
TOTAL COMPREHENSIVE INCOME FOR THE FINANCIAL YEAR AFTER TAX	**15,648**	**9,963**
a) Attributable to owners of the Bank	15,648	9,963

3. STATEMENT OF FINANCIAL POSITION

(in thousands of euros)

	Notes	As at 31 December	
		2016	2015
ASSETS			
Cash, cash balances at central banks and other demand deposits at banks	19	192,843	234,240
Financial assets held for trading:		64	91
- derivative financial instruments	20	64	91
Financial assets designated at fair value through profit or loss		136	222
Available-for-sale financial assets	21	354,615	330,088
Derivatives – hedge accounting	20	913	21
Loans and receivables:		1,726,905	1,654,741
- loans to banks	22	89,516	160,140
- loans to non-bank customers	23	1,626,373	1,482,682
- advances	24	11,016	11,919
Fair value changes of the hedged items in portfolio hedge of interest rate risk		45	-
Property, plant and equipment	25	18,700	21,523
Investment property	26	13,985	14,127
Intangible assets	27	4,068	4,471
Tax assets		-	1,246
- current tax assets		-	984
- deferred tax assets	36	-	262
Other assets	28	13,389	11,712
Total assets		**2,325,663**	**2,272,482**
LIABILITIES			
Financial liabilities held for trading:		-	1
- derivative financial instruments	20	-	1
Derivatives – hedge accounting	20	1,402	66
Financial liabilities measured at amortised cost:		2,017,524	1,971,643
- deposits from banks and central banks	29	62,700	22,821
- deposits from non-bank customers	30	1,839,935	1,776,685
- loans from banks and central banks	31	87,747	149,481
- loans from non-bank customers	32	28	60
- other financial liabilities	33	27,114	22,596
Fair value changes of the hedged items in portfolio hedge of interest rate risk		341	-
Provisions:		10,051	11,354
- provisions for liabilities and charges	34	5,193	6,754
- retirement benefit obligations	35	4,858	4,600
Tax liabilities:		1,603	-
- current tax liabilities		921	-
- deferred tax liabilities	36	682	-
Other liabilities	37	4,660	3,734
Total liabilities		**2,035,581**	**1,986,798**
EQUITY			
Share capital	38	22,173	22,173
Share premium	38	7,499	7,499
Accumulated other comprehensive income	39	5,859	10,451
Reserves from profit	40	229,362	227,654
Treasury shares	38	(49)	(49)
Retained earnings (including income for the current year)	40	25,238	17,956
Total equity		**290,082**	**285,684**
Total liabilities and equity		**2,325,663**	**2,272,482**

The accompanying notes on pages 42 to 101 are an integral part of the financial statements.

4. STATEMENT OF CHANGES IN EQUITY

(in thousands of euros)

For the year ended 31 December 2016	Notes	Share capital	Share premium	Accumulated other comprehensive income	Reserves from profit	Retained earnings or loss (including Income from the current year)	Treasury shares (equity deduction item)	Total equity
OPENING BALANCE FOR THE REPORTING PERIOD		**22,173**	**7,499**	**10,451**	**227,654**	**17,956***	**(49)**	**285,684**
Total comprehensive income for the year after tax		-	-	(4,592)	-	20,240	-	**15,648**
Dividends paid	40	-	-	-	-	(11,250)	-	**(11,250)**
Transfer of net profit to reserves from profit	40	-	-	-	1,708	(1,708)	-	**-**
CLOSING BALANCE		**22,173**	**7,499**	**5,859**	**229,362**	**25,238**	**(49)**	**290,082**
DISTRIBUTABLE PROFIT		-	-	-	-	19,228	-	**19,228**

(in thousands of euros)

For the year ended 31 December 2015	Notes	Share capital	Share premium	Accumulated other comprehensive income	Reserves from profit	Retained earnings or loss (including Income from the current year)	Treasury shares (equity deduction item)	Total equity
OPENING BALANCE FOR THE REPORTING PERIOD		**22,173**	**7,499**	**12,331**	**226,069**	**12,305***	**(49)**	**280,328**
Total comprehensive income for the year after tax		-	-	(1,880)	-	11,843	-	**9,963**
Dividends paid	40	-	-	-	-	(5,304)	-	**(5,304)**
Transfer of net profit to reserves from profit	40	-	-	-	1,585	(1,585)	-	**-**
Effect due to merger of Finor Leasing		-	-	-	-	697	-	**697**
CLOSING BALANCE		**22,173**	**7,499**	**10,451**	**227,654**	**17,956**	**(49)**	**285,684**
DISTRIBUTABLE PROFIT		-	-	-	-	11,947	-	**11,947**

*Retained earnings in the amount of euro 6,009 thousand arose from accounting differences in transition from local accounting standards to IFRS. Under the Management Board's decision this part of retained earnings it is not available for distribution to shareholders.

The accompanying notes on pages 42 to 101 are an integral part of the financial statements.

5. STATEMENT OF CASH FLOWS

(in thousands of euros)

	Notes	As at 31 December	
		2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES			
Total profit or loss before tax		22,959	14,198
Depreciation	13	4,692	5,422
Impairments / (reversal of impairments) of financial assets available-for-sale	15	299	-
Impairments / (reversal of impairments) of loans and receivables	15	20,385	14,892
Impairments of tangible assets, investment property, intangible assets and other assets	15	1,555	935
Net (gains) / losses from exchange differences		(209)	7,298
Net (gains) / losses from sale of tangible assets and investment properties		(1,043)	(47)
Other adjustments to total profit or loss before tax		(1,123)	(3,553)
Cash flow from operating activities before changes in operating assets and liabilities		**47,515**	**39,145**
(Increases) / decreases in operating assets (excl. cash & cash equivalents)		**(157,960)**	**(7,684)**
Net (increase) / decrease in financial assets held for trading		27	19
Net (increase) / decrease in financial assets designated at fair value through profit or loss		86	45
Net (increase) / decrease in financial assets available-for-sale		(27,878)	(33,804)
Net (increase) / decrease in loans and receivables		(124,243)	40,269
Net (increase) / decrease in assets-derivatives - hedge accounting		(937)	(21)
Net (increase) / decrease in other assets		(5,015)	(14,192)
Increases / (decreases) in operating liabilities		**47,664**	**(29,391)**
Net increase / (decrease) in financial liabilities held for trading		(1)	(147)
Net increase / (decrease) in deposits and loans measured at amortised cost		45,881	(31,367)
Net increase / (decrease) in liability – derivatives – hedge accounting		1,677	28
Net increase / (decrease) in other liabilities		107	2,095
Cash flow from operating activities		**(62,781)**	**2,070**
Income taxes (paid) / refunded		919	(1,502)
Net cash flow from operating activities		**(61,862)**	**568**
CASH FLOWS FROM INVESTING ACTIVITIES			
Receipts from investing activities		**1,434**	**14**
Receipts from the sale of property and equipment and investment properties		1,434	14
Cash payments on investing activities		**(900)**	**(3,906)**
Cash payments to acquire tangible assets and investment properties		(552)	(1,293)
Cash payments to acquire intangible assets		(348)	(2,613)
Net cash flow from investing activities		**534**	**(3,892)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Cash proceeds from financing activities		**-**	**-**
Cash payments on financing activities		**(11,250)**	**(5,304)**
Dividends paid		(11,250)	(5,304)
Net cash flow from financing activities		**(11,250)**	**(5,304)**
Effects of change in exchange rates on cash and cash equivalents		(513)	7,169
Net increase in cash and cash equivalents		**(72,578)**	**(8,628)**
Opening balance of cash and cash equivalents	42	264,453	265,912
Closing balance of cash and cash equivalents	42	**191,362**	**264,453**

(in thousands of euros)

Operational cash flows of interest and dividends	As at 31 December	
	2016	2015
Interest paid	(11,050)	(15,850)
Interest received	48,364	58,562
Dividends received	655	545

As at 31 December 2016, the Bank had undrawn credit lines and loans already committed of EUR 100,000 thousand (2015: nil).

The Bank has credit lines and other facilities of EUR 100,000 thousand that are available for financing future business operations without any restrictions.

The accompanying notes on pages 42 to 101 are an integral part of the financial statements.

Notes To Financial Statements

1. GENERAL INFORMATION

Banka Koper d.d. is a public limited company with the head office at 14 Pristaniška Street, Koper/Capodistria (hereinafter referred to as Banka Koper d.d. or the Bank). Since 2002, Banka Koper d.d. is member of the Intesa Sanpaolo Group (originally SanpaoloIMI), one of the leading banking groups in Italy. As of January 1 1 2007, the Sanpaolo IMI Group merged with Banca Intesa. Banka Koper d.d. is owned directly by the bank Intesa Sanpaolo. It has a head office in Piazza San Carlo 166, Turin, Italy and a secondary office in Via Monte di Pietá8, Milan, Italy.

In accordance with the third paragraph of article 3 and the first paragraph of article 4 of the Regulation on the criteria for determining whether a bank is considered significant (Official Gazette of the Republic of Slovenia, No. 14/15; hereinafter referred to as the Regulation on the criteria), Banka Koper d.d. is a significant bank in the Republic of Slovenia. As a significant bank, Banka Koper d.d. shall comply with all the requirements specified as mandatory in the relevant provisions laid down in the Banking Act (Official Gazette of the Republic of Slovenia, No. 25/2015; hereinafter referred to as at Banking Act (ZBan-2), i.e. and the Regulation (EU) No. 575/2013 and in the first paragraph of article 1 of the Regulation on the criteria. The Bank shall comply with the following requirements:

- The conditions for the members of the governing body of a significant bank that hold several directorships at the same time (the third paragraph of article 36 of the Banking Act (ZBan-2);
- Establishing a compliance department (the first paragraph of Article 146 of the Banking Act (ZBan-2);
- The quantitative information shall be made available to the public at the level of the bank's members of the management body (the second paragraph of article 450 of the Regulation (EU) No. 575/2013);
- Significant subsidiaries of EU parent financial holding companies or EU parent mixed holding companies and those subsidiaries which are of material significance for their local market shall disclose the information on an individual or sub-consolidated basis (article 13 of the Regulation (EU) No. 575/2013), and namely regarding the bank's own funds (article 437), capital requirements (article 438), capital buffers (article 440), credit risk adjustments (article 442), remuneration policy (article 450), leverage (article 451), and the use of credit risk mitigation techniques (article 453).

The above requirements to make disclosures are disclosed in a separate report named Additional information for the financial year 2016.

The Bank prepares its financial statements as at the last day of the calendar year.

The date of the Management Board statement shall be considered as the date on which the financial statements were approved.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted for the preparation of the financial statements are set out below:

2.1 BASIS OF PREPARATION

Statement of compliance
The financial statements for 2016 have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.

Basis of measurement
The financial statements have been prepared under the historical cost convention and modified by the revaluation of available-for-sale investment securities, financial assets and financial liabilities at fair value through profit or loss, and derivative contracts at fair value.

Use of estimates and judgements
The preparation of financial statements in conformity with IFRS as adopted by the EU requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from those estimates.

Use of estimates and judgements are applied for:
- Impairment of loans and advances
- Fair value of financial instruments
- Impairment of instruments available-for-sale
- Impairment of real estate inventory obtained for the repayment of loans collateralised by pledging real estate.

A more detailed disclosures is shown under chapter 2.11 Impairment of financial assets and 3.3 Credit risk.

The accounting policies used are consistent with those applied in the financial statements for the previous year.

Current list of new EU IFRS Standards, Interpretations and amendments to published Standards (as at 24 January 2017) that are not yet effective, for disclosure in financial statements prepared in accordance with IFRS as adopted by the European Union (EU) for the annual reporting period ended 31 December 2016.

The following new Standards, interpretations and amendments are not yet effective for the annual reporting period ended 31 December 2016 and have not been applied in preparing these financial statements: [IAS 8.30 (a)].

Standard/Interpretation [IAS 8.31 (a), 8.31(c)]	**Nature of impending change in accounting policy [IAS 8.31 (b)]**	**Example wording regarding the possible impact on financial statements [IAS 8.30 (b); 31 (e)]**
IFRS 9 Financial Instruments (2014) (Effective for annual periods beginning on or after 1 January 2018; to be applied retrospectively with some exemptions. The restatement of prior periods is not required, and is permitted only if information is available without the use of hindsight. Early application is permitted.)	This Standard replaces IAS 39, Financial Instruments: Recognition and Measurement, except that the IAS 39 exception for a fair value hedge of an interest rate exposure of a portfolio of financial assets or financial liabilities continues to apply, and entities have an accounting policy choice between applying the hedge accounting requirements of IFRS 9 or continuing to apply the existing hedge accounting requirements in IAS 39 for all hedge accounting. Although the permissible measurement bases for financial assets – amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit and loss (FVTPL) – are similar to IAS 39, the criteria for classification into the appropriate measurement category are significantly different. A financial asset is measured at amortized cost if the following two conditions are met: - the assets is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and, - its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding. In addition, for a non-trading equity instrument, a company may elect to irrevocably present subsequent changes in fair value (including foreign exchange gains and losses) in OCI. These are not reclassified to profit or loss under any circumstances. For debt instruments measured at FVOCI, interest revenue, expected credit losses and foreign exchange gains and losses are recognised in profit or loss in the same manner as for amortised cost assets. Other gains and losses are recognised in OCI and are reclassified to profit or loss on derecognition. The impairment model in IFRS 9 replaces the ‘ incurred loss’ model in IAS 39 with an ‘ expected credit loss’ model, which means that a loss event will no longer need to occur before an impairment allowance is recognised. IFRS 9 includes a new general hedge accounting model, which aligns hedge accounting more closely with risk management. The types of hedging relationships – fair value, cash flow and foreign operation net investment – remain unchanged, but additional judgment will be required. The standard contains new requirements to achieve, continue and discontinue hedge accounting and allows additional exposures to be designated as hedged items. Extensive additional disclosures regarding an entity’s risk management and hedging activities are required.	Based on its preliminary assessment, the Bank, as a bank, expects that substantially all of financial assets classified as loans and receivables under IAS 39 will continue to be measured at amortised cost under IFRS 9. At this stage it is quite clear what portion of the Bank’s debt securities will be measured at FVOCI. This determination is the result of the business model test outcome. It is expected that all AFS debt securities will be reclassified under IFRS 9 into FVOCI. It is also possible that a number of equity instruments currently classified as available for sale will be measured at FVTPL under IFRS 9, but this determination will depend on an election to be made by the entity at the date of initial application – that is 1 January 2018. The Bank has not yet decided how it will classify these instruments. It is expected that deposits from customers will be continued to be measured at amortised cost under IFRS 9. It is expected that the new expected credit loss model under IFRS 9 will accelerate the recognition of impairment losses and lead to higher impairment allowances at the date of initial application. The Bank is not yet able to quantify the expected impact that the initial application of IFRS 9 will have on its IFRS statements.
IFRS 15 Revenue from contracts with customers (Effective for annual periods beginning on or after 1 January 2018. Earlier application is permitted.) Clarifications to IFRS 15 Revenue from Contracts with Customers is not yet endorsed by the EU but IFRS 15 Revenue from Contracts with Customers including Effective Date of IFRS 15 have been endorsed by the EU.	The new Standard provides a framework that replaces existing revenue recognition guidance in IFRS. Entities will adopt a five-step model to determine when to recognise revenue, and at what amount. The new model specifies that revenue should be recognised when (or as) an entity transfers control of goods or services to a customer at the amount to which the entity expects to be entitled. Depending on whether certain criteria are met, revenue is recognised: - over time, in a manner that depicts the entity’s performance; or - at a point in time, when control of the goods or services is transferred to the customer. IFRS 15 also establishes the principles that an entity shall apply to provide qualitative and quantitative disclosures which provide useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from a contract with a customer.	The Bank is not yet able to quantify the expected impact that the initial application of IFRS 15 will have on its IFRS statements. Although it has not yet fully completed its initial assessment of the potential impact of IFRS 15 on the Bank’s financial statements, management does not expect that the new Standard, when initially applied, will have material impact on the Bank’s financial statements. The timing and measurement of the Bank’s revenues are not expected to change under IFRS 15 because of the nature of the Bank’s operations and the types of revenues it earns.

Standard/Interpretation [IAS 8.31 (a), 8.31(c)]	Nature of impending change in accounting policy [IAS 8.31 (b)]	Example wording regarding the possible impact on financial statements [IAS 8.30 (b); 31 (e)]
IFRS 16 Leases (Effective for annual periods beginning on or after 1 January 2019. Earlier application is permitted if the entity also applies IFRS 15.) This pronouncement is not yet endorsed by the EU.	IFRS 16 supersedes IAS 17 Leases and related interpretations. The Standard eliminates the current dual accounting model for lessees and instead requires companies to bring most leases on-balance sheet under a single model, eliminating the distinction between operating and finance leases. Under IFRS 16, a contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration. For such contracts, the new model requires a lessee to recognise a right-of-use asset and a lease liability. The right-of-use asset is depreciated and the liability accrues interest. This will result in a front-loaded pattern of expense for most leases, even when the lessee pays constant annual rentals. The new Standard introduces a number of limited scope exceptions for lessees which include: - leases with a lease term of 12 months or less and containing no purchase options, and - leases where the underlying asset has a low value (‘ small-ticket’ leases). Lessor accounting shall remain largely unaffected by the introduction of the new Standard and the distinction between operating and finance leases will be retained.	The Bank does not expect that the new Standard, when initially applied, will have material impact on the financial statements because the Bank is not party to a contractual arrangement that would be in the scope of IFRS 16.
Amendments to IFRS 2: Classification and Measurement of Share-based Payment Transactions (Effective for annual periods beginning on or after 1 January 2018; to be applied prospectively. Early application is permitted.) This pronouncement is not yet endorsed by the EU.	The amendments clarify share-based payment accounting on the following areas: - the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments; - share-based payment transactions with a net settlement feature for withholding tax obligations; and - a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity settled.	The Bank expects that the amendments, when initially applied, will not have a material impact on the presentation of the financial statements of the bank because the Bank does not enter into share-based payment transactions.
Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Effective for annual periods beginning on or after 1 January 2021; to be applied prospectively.) This pronouncement is not yet endorsed by the EU.	The amendments address concerns arising from implementing IFRS 9 before implementing the replacement standard that the IASB is developing for IFRS 4. The amendments introduce two optional solutions. One solution is a temporary exemption from IFRS 9, effectively deferring its application for some insurers. The other is an overlay approach to presentation to alleviate the volatility that may arise when applying IFRS 9 before the forthcoming insurance contracts standard.	The Bank is not an insurance provider, therefore does not expect any material impact on the financial statements of the Bank.
Amendments to IFRS 10 and IAS 28 Sale or contribution of assets between an investor and its associate or joint venture (The effective date has not yet been determined by the IASB, however earlier adoption is permitted.)	The Amendments clarify that in a transaction involving an associate or joint venture, the extent of gain or loss recognition depends on whether the assets sold or contributed constitute a business, such that: - a full gain or loss is recognised when a transaction between an investor and its associate or joint venture involves the transfer of an asset or assets which constitute a business (whether it is housed in a subsidiary or not), while - a partial gain or loss is recognised when a transaction between an investor and its associate or joint venture involves assets that do not constitute a business, even if these assets are housed in a subsidiary.	The Bank does not expect that the amendments, when initially applied, will have material impact on the financial statements.

Standard/Interpretation [IAS 8.31 (a), 8.31(c)]	Nature of impending change in accounting policy [IAS 8.31 (b)]	Example wording regarding the possible impact on financial statements [IAS 8.30 (b); 31 (e)]
Amendments to IAS 7 (Effective for annual periods beginning on or after 1 January 2017, to be applied prospectively. Early application is permitted.) This pronouncement is not yet endorsed by the EU.	The amendments require new disclosures that help users to evaluate changes in liabilities arising from financing activities, including changes from cash flows and non-cash changes (such as the effect of foreign exchange gains or losses, changes arising for obtaining or losing control of subsidiaries, changes in fair value).	The Bank expects that the amendments, when initially applied, will not have a material impact on the presentation of the financial statements of the Bank.
Amendments to IAS 12: Recognition of Deferred Tax Assets for Unrealised Losses (Effective for annual periods beginning on or after 1 January 2017; to be applied prospectively. Early application is permitted.) This pronouncement is not yet endorsed by the EU.	The amendments clarify how and when to account for deferred tax assets in certain situations and clarify how future taxable income should be determined for the purposes of assessing the recognition of deferred tax assets.	The Bank expects that the amendments, when initially applied, will not have a material impact on the presentation of the financial statements of the Bank because the Bank already measures future taxable profit in a manner consistent with the Amendments.
Amendments to IAS 40 Transfers of Investment Property (Effective for annual periods beginning on or after 1 January 2018; to be applied prospectively.) This pronouncement is not yet endorsed by the EU.	The amendments reinforce the principle for transfers into, or out of, investment property in IAS 40 Investment Property to specify that such a transfer should only be made when there has been a change in use of the property. Based on the amendments a transfer is made when and only when there is an actual change in use – i.e. an asset meets or ceases to meet the definition of investment property and there is evidence of the change in use. A change in management intention alone does not support a transfer.	The Bank does not expect that the amendments will have a material impact on the financial statements because [the Bank transfers a property asset to, or from, investment property only when there is an actual change in use/the entity does not have investment property].
IFRIC 22 Foreign Currency Transactions and Advance Consideration (Effective for annual periods beginning on or after 1 January 2018). This pronouncement is not yet endorsed by the EU.	The Interpretation clarifies how to determine the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration in a foreign currency. In such circumstances, the date of the transaction is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration.	The Bank does not expect that the Interpretation, when initially applied, will have material impact on the financial statements as the Bank uses the exchange rate on the transaction date for the initial recognition of the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration.

Annual improvements to IFRSs

Annual improvements to IFRSs 2014-2016 cycle were issued on 8 December 2016 and introduce two amendments to two standards and consequential amendments to other standards and interpretations that result in accounting changes for presentation, recognition or measurement purposes. The amendments on IFRS 12 Disclosure of Interest in Other Entities are effective for annual periods beginning on or after 1 January 2017 and amendments on IAS 28 Investments in Associates and Joint Ventures are effective for annual periods beginning on or after 1 January 2018; to be applied retrospectively. Earlier application is permitted.

The improvements introduce two amendments to two standards and consequential amendments to other standards and interpretations that result in accounting changes for presentation, recognition or measurement purposes. These amendments are applicable to annual periods beginning on or after either 1 January 2017 or 1 January 2018; to be applied retrospectively.
None of these amendments are expected to have a significant impact on the financial statements of the Bank.

2.2 FOREIGN CURRENCY TRANSLATION

Functional and presentation currency
Items included in the financial statements are measured using the currency of the primary economic environment in which the Bank operates ('the functional currency'). The financial statements are presented in euros, which is the Bank's functional and presentation currency.

Recording foreign currency transactions
Foreign currency transactions are translated into the functional currency using the exchange rate prevailing at the date of transactions. Exchange rate differences resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Translation differences on non-monetary items, such as equities at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items, such as equities classified as available-for-sale, are included in the fair value reserve in equity.
Income and expenses arising on foreign currencies are translated at the exchange rate at the date of the transaction. Gains and losses resulting from buying and selling foreign currencies for trading purposes are reported in profit or loss as net gains or losses from trading of foreign currencies.

2.3 RELATED PARTIES

For the purposes of the financial statements, related parties include all entities, that directly or indirectly, through one or more intermediaries, control or are controlled by, or are under common control with, the reporting enterprise. Related parties include parents, subsidiaries, fellow subsidiaries, associates of the reporting entity, members of the key management personnel and directors of the Banks and enterprises over which the key management personnel and directors of the reporting entity are able to exercise significant influence (participation in making financial and operating policy decisions of an enterprise).

2.4 FINANCIAL ASSETS

Classification

a) Financial assets at fair value through profit or loss
This category has two sub-categories: financial instruments held for trading and financial instruments designated at fair value through profit or loss at inception. Financial instruments are classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are classified as held for trading unless they are designated as hedges.

b) Loans and receivables
Loans and receivables are non-derivative financial instruments with fixed or determinable payments that are not quoted in an active market, other than:
(a) those that the entity intends to sell immediately or within the short term, which are classified as held for trading and those that the entity designates at fair value through profit or loss upon initial recognition;
(b) those that the entity, upon initial recognition, designates as available for sale; or
(c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration

c) Available-for-sale financial assets
Available-for-sale financial assets are non-derivative financial assets that are designated as available for sale or that are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss.

Recognition and measurement

a) Date of recognition
Purchases and sales of financial instruments at fair value through profit or loss, held to maturity and available-for-sale are recognised on the trade date. Loans are recognised when the cash is advanced to the borrowers.

b) Value of recognition and subsequent measurement
Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit and loss.

Financial assets at fair value through profit or loss and available-for-sale financial assets are measured subsequently at fair value. Gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss are presented in the income statement in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in other comprehensive income, until the financial asset is disposed of, derecognised or impaired, at which time the cumulative gain or loss previously recognised in other comprehensive income is recognised in profit or loss. However, interest calculated using the effective interest method and foreign currency gains and losses on monetary assets classified as available-for-sale are recognised in profit or loss. Dividends on available-for-sale equity instruments are recognised in profit or loss when the entity's right to receive payment is established.
Loans and receivables financial assets are carried at amortised cost.

Restructured loans

Due to inability of the client to repay the debt under the originally agreed terms, where possible, the Bank seeks to restructure performing loans or non-performing loans (substandard, doubtful or past due by more than 90 days) rather than start recovery of collateral due to long-lasting procedures, high court costs and in view of the possibility of restoring the credit worthiness of the borrower. Bank restructuring includes one or more activities: extending the payment arrangements and/or reduction of interest rate and/or partial write-off and/or (exceptionally) debt to equity swap. The de-recognition of the previous loan is exercised when terms and condition of the restructured loan significantly deviate from the original one. Once the terms have been renegotiated and annexes are concluded, the loan is no longer considered past due. However, the client remains classified in non-performing category for at least 1 year and only after that period it can be transferred to performing category. Subsequently it will remain in a probation status for at least 2 years. The management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur.

De-recognition of financial instruments

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or the financial asset is transferred and the transfer meets criteria for de-recognition.

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- The rights to receive cash flows from the asset have expired; or
- The Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under an assignment arrangement; and either:
    - The Bank has transferred substantially all the risks and rewards of the asset, or
    - The Bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Bank has transferred its rights to receive cash flows from an asset or has entered into an assignment arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset. In that case, the Bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Bank has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a de-recognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in income statement.

Fair value measurement principles

The fair value of financial instruments is based on their quoted market price at the reporting date. If a quoted market price is not available, the fair value of the instruments is estimated using discounted cash flow techniques or pricing models.
Where discounted cash flow techniques are used, estimated future cash flows are based on the best estimates and the discount rate is a market related rate at the reporting date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the reporting date, where possible, but where this is not feasible, the best information available is used.

Since the application of IFRS 13 – Fair value measurement, the inputs used to measure fair value, should be presented when classifying financial instruments in the three levels of fair value hierarchy:

- **Level 1 inputs:** Fair value measured using (unadjusted) quoted prices in active markets for identical assets or liabilities.
- **Level 2 inputs:** Fair value measured using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices from similar assets) or indirectly (i.e. derived from prices of similar instruments).
- **Level 3 inputs:** Fair value measured using inputs for the asset or liability that are not based on observable market inputs.

More detailed disclosure is shown under chapter 3.9 Fair value of assets and liabilities.

2.5 OFFSETTING OF FINANCIAL ASSETS AND LIABILITIES

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

2.6 DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments fall into the following categories: forward-based, swap-based and option-based., are measured initially at fair value. Subsequent to initial recognition all derivatives are measured considering changes in fair value. To determine their fair value, derivative financial assets and financial liabilities are measured using quoted prices, discounted cash flow models or pricing models, as appropriate. All derivatives are carried at their fair value as assets when favourable to the Bank, and as liabilities when unfavourable to the Bank.
Certain derivative financial instruments that provide effective economic hedges and are not qualified for hedge accounting under the specific accounting rules, are therefore accounted for as derivative financial instruments held for trading purposes.

The best evidence of the fair value of a derivative financial instrument at initial recognition is the transaction price (the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions of the same instrument (without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Bank recognises profits/losses on Day 1; if not, profits/losses are not recognised on Day 1, but if and when such evidence becomes available or when the derivative is derecognised.

De-recognition of the derivatives occurs only when through a legal transaction that transfers ownership of a financial instrument to the buyer, the seller has also transferred substantially all the risks and future rewards of ownership of the financial instrument.

2.7 HEDGE ACCOUNTING

The Bank uses derivative financial instruments to manage its exposures to interest rate risk. Such derivative financial instruments are initially recognised at fair value on the date on which they are entered to and are subsequently re-measured at fair value. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

For the purpose of hedge accounting, hedges could refer to:

- Fair value hedge – a hedge of exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment;
- Cash flow hedge – a hedge of the exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction;
- Hedge of a net investment in a foreign currency.

At the inception of a hedge relationship, the Bank formally designates and documents the hedge relationship to which the Bank wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the Bank will assess the effectiveness of changes in the hedging instrument's fair value in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are tested regularly throughout their life to determine that they actually have been highly effective throughout the financial reporting periods for which they are designated.

The Bank uses fair value hedge to cover exposure to changes in the fair value attributable to the different risk categories of assets and liabilities in the statement of financial position, or a portion of these or to cover portfolios of financial assets and liabilities.

2.8 INTEREST INCOME AND EXPENSE

Interest income and expense are recognised in profit or loss for all interest-bearing instruments on an accrual basis using the effective interest method based on the actual purchase price. Interest income includes coupons earned on fixed income investments and accrued discounts and premium on securities. Once a financial asset or group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the expected estimated future cash payments and receipts for the purpose of measuring the impairment loss.
The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant lifetime of financial instrument. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument (e. e.g., prepayment options, call options and similar options) but does not consider future credit losses. The calculation includes all fees and margins paid or received between parties to the contract that are an integral part of the effective interest rate, such as transaction costs and all other premiums or discounts.

2.9 FEE AND COMMISSION INCOME

Fees and commissions are generally recognised as the services are provided. Fees and commissions consist mainly of fees charged on payment services, credit cards, services and fund management on behalf of legal entities and citizens, together with commissions from guarantees. For loan commitments the bank charged the client for small administrative expenses for loan elaboration, which cover just the process costs. Subsequently the loan management fee is collected promptly (each month for loan, each trimester for guaranties). These fees cover process costs as well. Fees receivable that represent a return for services provided are in income statement netted of tax on financial services.

2.10 SALE AND REPURCHASE AGREEMENTS

Securities sold subject to sale and repurchase agreements ('repos') continue to be recognised in the financial statements of the temporary seller, with the counterparty liability included in deposits from banks or customers as appropriate. Securities sold, subject to sale and repurchase agreements are reclassified in the financial statements as pledged assets when the transferee has the right by contract or custom to sell or re-pledge the collateral. Securities purchased under agreements to resell ('reverse repos') are recorded as loans and advances to other banks or customers, as appropriate.

The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

2.11 IMPAIRMENT OF FINANCIAL ASSETS

a) Loans and other assets carried at amortised cost

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset ('a loss event') and that loss event (or events) has an impact on the estimated future cash flows.
The Bank first assess whether objective evidence of impairment exists for financial assets that are individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset it includes the asset in a group of financial assets with similar credit risk characteristic and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment.
If there is objective evidence that an impairment loss on loans and receivables or held to maturity investment has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate (in case of a variable interest rate, the last effective interest rate is taken). The carrying amount of the asset is reduced through the adjustment account and the amount of the loss is recognised in the income statement.
The calculation of present value of the estimated future cash flows of collateralised financial assets reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (on the basis of the Bank's internal classification process that considers all relevant factors).
Future cash flows for the group of individually significant financial assets that are evaluated for impairment are estimated on the basis of the contractual cash flows and historical loss experience for assets with credit risk characteristics similar to those in the group. The methodology and assumptions used for estimating future cash flows are reviewed regularly.
If the amount of the impairment subsequently decreases due to an event occurring after the write down, the reversal of loss is credited as a reduction of the adjustment account for loan impairment.

When a loan is uncollectible, it is written off against the related provision for loan impairment. In the case that the provision for loan impairment does not exist, the write off is recognised directly in the income statement under gains less losses from financial assets and liabilities not recognised at fair value through profit or loss. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are shown as income in income statement.

b) Assets carried at fair value

At each reporting date the Bank assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value is considered when the investment is below its cost value. In line with Intesa Sanpaolo Group accounting policies, a significant decrease is when the financial instrument's fair value decreases by more than 30% below its average initial carrying amount. A prolonged decline in the asset's fair value generally occurs when the fair value of a financial instrument has been below its average initial carrying amount for at least 24 months. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the initial carrying amount and current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from other comprehensive income and recognised in the income statement. Impairment losses on equity instruments recognised in the income statement are not reversed through the income statement but always recognised as increase in other comprehensive income. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the income statement.

2.12 INTANGIBLE ASSETS

Intangible assets encompass licences for computer software, patents, copyrights and other industrial property rights acquired, and development expenditures, are carried in the statement of financial position at cost less any accumulated amortisation and any accumulated impairment losses.
Expenditure on research and development and maintaining computer software is recognised in profit or loss as the expense is incurred. In circumstances when expenditure is directly associated with the development of computer software that will probably generate expected future economic benefits exceeding costs, expenditures are recognised as intangible assets. Directly attributable costs include administrative expenses related to software development, as well as part of relevant overhead costs.

The amortisation method used to allocate the depreciable amount of an asset on a systematic basis over its useful life is the straight-line method. Amortisation begins when the asset is available for use.

The Bank reviews the amortisation period and the amortisation method for an intangible asset with a finite useful life at each financial year-end.

Intangible assets	Estimated useful lives in 2016	Estimated useful lives in 2015
Licence fees	4	4
Research and development expenditure	5	4
Computer software	4	4

Gains and losses arising on de-recognition should be calculated as the difference between the asset's net disposal proceeds and its carrying amount and should be recognised in the income statement. Intangible assets are assessed for impairment whenever there is an indication that the intangible asset may be impaired. The assessment for impairment is carried out at least on yearly bases.

2.13 INVESTMENT PROPERTY

Investment property is property (land or a building) held to earn rentals or for capital appreciation or both, rather than for use in the supply of services in the ordinary course of business.

An investment property is measured initially at its cost. The costs included in the initial measurement, comprises its purchase price and any directly attributable expenditure.
After initial recognition, the Bank carries investment at cost less accumulated depreciation and accumulated impairment losses, if any.
Investment property items are depreciated over their useful lives and are submitted to valuation by an independent appraiser. The Bank applies the same depreciation method and depreciation rates as for the buildings it uses in the ordinary course of business (note 2.14).

2.14 PROPERTY, PLANT AND EQUIPMENT

Tangible fixed assets are land, buildings, manufacturing plant and equipment. An item of property, plant and equipment that qualifies for recognition as an asset shall be initially measured at its cost. The cost of an item of property, plant and equipment comprises its purchase price after deducting trade discounts, including import duties and non-refundable purchase taxes, directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating (cost of transport, installation …) and the cost of its dismantlement, removal and restoration. The cost of interest related to the acquisition of an item of property, plant and equipment is included in the cost of acquiring that item and capitalised.
The Bank measures a property, plant and equipment item acquired in exchange for a non-monetary asset or a combination of monetary and non-monetary assets at fair value.

The Bank assesses annually whether there is any indication that an asset may be impaired. If there is an indication that an asset may be impaired, the recoverable amount of the asset is determined. The recoverable amount is the higher of the fair value less costs to sell and the value in use. If the recoverable amount exceeds the carrying amount, it is an indication that the asset is not impaired.
The Bank recognises subsequent costs in the carrying amount of an item of property, plant and equipment when it is probable that future economic benefits associated with the item will flow to the Bank. The costs of day-to-day

servicing (repairs and maintenance) are recognised in profit or loss as incurred.

Depreciation charges are calculated by using the straight-line method. The depreciation rates are determined to allocate the value of items of property, plant and equipment over their estimated useful lives to expenses.
Assets in the course of transfer or construction are not depreciated until they are brought into use.
The residual value and the useful life of an asset is reviewed on a regular basis and, if expectations differ from previous estimates, the change(s) is accounted for as a change in an accounting estimate.

Property, plant and equipment	Estimated useful lives in 2016	Estimated useful lives in 2015
Buildings	16.6-40	16.6-40
Other investment in intangibles	10	10
Equipment	5	5
Motor vehicles	5	5
Computers and software	4	4

Any gain or loss on disposal of an item of property, plant and equipment determined as the difference between the proceeds and the carrying amount are recognised in profit or loss, determining operating profit.

2.15 ACCOUNTING FOR LEASES

Determining whether an arrangement is, or contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

The Bank as lessee
Leases which do not transfer to the Bank substantially all the risks and rewards incidental to ownership of the leased items are operating leases. Lease payments under operating lease are recognised as an expense in profit or loss on a straight line basis over the lease term. Contingent rents are charged as expenses in the periods in which they are incurred

A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership to the lessee. An item of property, plant and equipment acquired by way of finance lease is recorded as an asset and a liability at the lower of the fair value of the asset and the present value of the minimum lease payments at the commencement of the lease term, less accumulated depreciation and any impairment losses. An item of property, plant and equipment acquired under a finance lease is depreciated over the useful life of the asset. If there is no reasonable certainty that the lessee will obtain ownership of the leased asset by the end of the lease term, the leased assets shall be fully depreciated over the shorter of the lease term and its useful life.

The Bank as lessor
When assets are leased under an operating lease, the Bank recognises rental income in the income statement on a straight-line basis over the period of the lease.

When assets are leased out under a finance lease, the present value of the lease payments is recognised as a receivable. Income from finance leasing transactions is apportioned systematically over the primary lease period, reflecting a constant periodic return on the lessor's net investment outstanding.

2.16 CASH AND CASH EQUIVALENTS

For the purpose of the cash flow statement, cash and cash equivalents comprise cash on hand and balances held with central banks except for obligatory reserves, securities held for trading, loans to banks and debt securities not held for trading with original maturity up to 90 days.

2.17 FINANCIAL LIABILITIES

Loans received deposits repayable and debt securities issued are recognised in the statement of financial position in the amount of the funds received less direct transaction costs. The loans received, deposits repayable and debt securities issued are measured at amortised cost and the difference between the initial amount and the end amount is transferred to the income statement using the effective interest method.

2.18 PROVISIONS

Provisions are recognised in respect of present obligations arising from past events where it is probable that outflows of resources embodying past economic benefits will be required to settle the obligation; and they can be reliably estimated.

2.19 FINANCIAL GUARANTEES

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument. Financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.
Financial guarantee liabilities are initially recognised in the financial statements at their fair value on the date the guarantee is given. Subsequent to initial recognition, the Bank's liabilities under such guarantees are measured at the higher of the initial measurement, less amortisation calculated to recognise in the income statement the fee income earned on a straight line basis over the period, and the best estimate of the expenditure required to settle any financial obligation arising as the result of the guarantees at the reporting date. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the management's judgment.

2.20 INCOME TAX

Current income tax has been calculated in accordance with the local tax law and using the tax rate of 17%. With the year 2017 the corporate income tax will increase to 19%.
Deferred income tax is calculated for all taxable temporary differences using the tax rate of 19%. Temporary differences are differences between the carrying amount of an asset or liability in the statement of financial position and its tax base. The tax rates (and tax laws) that have been enacted by the end of the reporting date are used to determine deferred income tax. The principal temporary differences arise from the valuation of financial instruments including derivatives and provisions for retirement benefit obligations. A deferred tax asset shall be recognised for the carry forward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilised. Deferred tax related to fair value re-measurement of available-for-sale investments is charged or credited directly to other comprehensive income and is subsequently, when the financial asset is sold or de-recognised, recognised in the income statement together with the gain or loss from disposal.
An entity shall recognise a deferred tax liability or asset for all taxable temporary differences associated with investments in subsidiaries, branches and associates, and interests in joint ventures, except to the extent that both of the following conditions are satisfied: the parent, investor or venturer is able to control the timing of the reversal of the temporary difference; and it is probable that the temporary difference will not reverse in the foreseeable future.

2.21 EMPLOYEE BENEFITS

Employee benefits include jubilee benefits, retirement indemnity bonuses and other long-service benefits. According to Slovenian legislation, employees retire after 40 years of services, when, if fulfilling certain conditions, they are entitled to a termination benefit paid out as a lump sum. Valuations of these obligations are carried out by independent qualified actuaries, by using the book reserve method.

The Bank's obligation for the current service cost of providing pension benefits and the increment in the present value of the defined benefit obligation due to the approaching beginning of the defined benefit liability (interest cost) was assessed. The increase in the benefit scheme liabilities in excess of the above two assessments shall be recognised as the actuarial gain or loss.

The defined benefit scheme liabilities are measured on an actuarial basis using the projected unit credit method, which measures actuarial liabilities in accordance with the expected wage/salary increase from the valuation date until the foreseen retirement of the employed person. The wage/salary increase comprises promotion and inflation-related rise.

Under IAS19, the calculated current scheme liabilities are discounted using the rates equivalent to the market yields at the balance-sheet date on high-quality corporate bonds that are denominated in the currency in which the benefits will be paid by the employer. Since there is no deep market in such bonds in the Republic of Slovenia, the discount rate is determined by reference to market yields on government bonds.
For the calculation of actuarial gains and losses, the following assumptions have been used:
- The discount rate of 1.02% (2015: 1.9%), and
- Future salary increases of 0% p.a. for 2017 and 0.9% p.a. from 2018 onwards (2015: nil).

2.22 SHARE CAPITAL

Dividends on ordinary shares
Dividends payable to the holders of ordinary shares lower the equity in the period in which the declaration of the dividend is approved by Bank's owners.

Treasury shares
If the Bank repurchases its own equity instruments (treasury shares), the cost of the shares it has reacquired is deducted from equity. In case that the Bank subsequently sells its treasury shares, the consideration received is recognised directly in equity.

2.23 FIDUCIARY ACTIVITIES

The Bank acts as an intermediary on behalf and for account of customers who want to underwrite units of investment funds. A fee is charged for this service. These assets are not shown in the statement of financial position.

2.24 COMPARATIVE INFORMATION

The same accounting policies as for the reporting period have been applied for the comparative information for the prior reporting period.

3. RISK MANAGEMENT ORGANISATION

The risk management policies and their implementation in the Bank's operational processes are of high importance for a sound business activity. The Bank has harmonised its risk management process with the risk management framework of the parent Group Intesa Sanpaolo. Therefore, risk management is governed in accordance with the Group best practices, which require a strong institution-wide risk culture involving Bank's management at all levels, and an independent risk management function.

The risk management process is divided in several stages, starting with the risk identification and measurement, which allows the Bank to understand the different types of risk, to measure its potential impact and to recognise in advance possible trends that can significantly change its business environment. The second step is the management of risk, whereby the Bank has to undertake strategic decisions on the type and the level of risk to be assumed, to establish whether to mitigate, diversify or reduce risk exposure and to establish risk limits in line with the Bank's risk capacity and risk appetite. Once risk has been assumed, it shall be properly overseen, which means monitoring risk tolerance limits and reporting to the Bank's governing bodies.

The most important risks in terms of Bank's total exposure are credit risk, interest rate risk, liquidity risk and operational risk. In the course of 2016, the Bank strengthened the credit quality control system with further alignment with policies and procedures of Intesa Sanpaolo Group, by improving the existing control environment and implementing new controls.

3.1 CORPORATE RISK MANAGEMENT AND ORGANIZATIONAL STRUCTURE

3.1.1 Corporate risk management

The following structures take part in the risk governance process:

The Supervisory Board approves the strategic directions and risk management policies and reviews the efficiency and adequacy of the overall risk management process within the Bank.

The Risk Committee is an advisory body to the Supervisory Board, which provides advice regarding the Bank's current and future propensity to assume risk and provides assistance in the supervision of senior management with respect to the implementation of the risk management strategy.

The Audit Committee is an advisory body to the Supervisory Board with responsibility to give recommendations and advice to the Board in particular on matters relating to evaluation of the adequacy and efficiency of the Bank's entire system of internal controls over financial reporting including oversight of exposure to risk.

The Management Board is responsible for the implementation of risk management policies and internal controls; it establishes organisational and other conditions for the execution of risk policies and controls.

The Asset and Liability Committee (ALCO) evaluates the exposure to financial risks and give guidance about measures necessary to manage financial exposures.

The Asset Quality Board monitors the loan portfolio and its quality and takes necessary measures in order to prevent and mitigate lending losses.

The Internal Audit Department evaluates and reviews processes, procedures, guidelines, policies and all operating activities performed by the Bank with the aim to evaluate the efficiency and effectiveness of the internal controls system and risk management system.

The Compliance and AML Department assesses and manages compliance risk in relation to domestic and international rules and internal acts in order to prevent legal sanctions, financial losses and reputational risk.

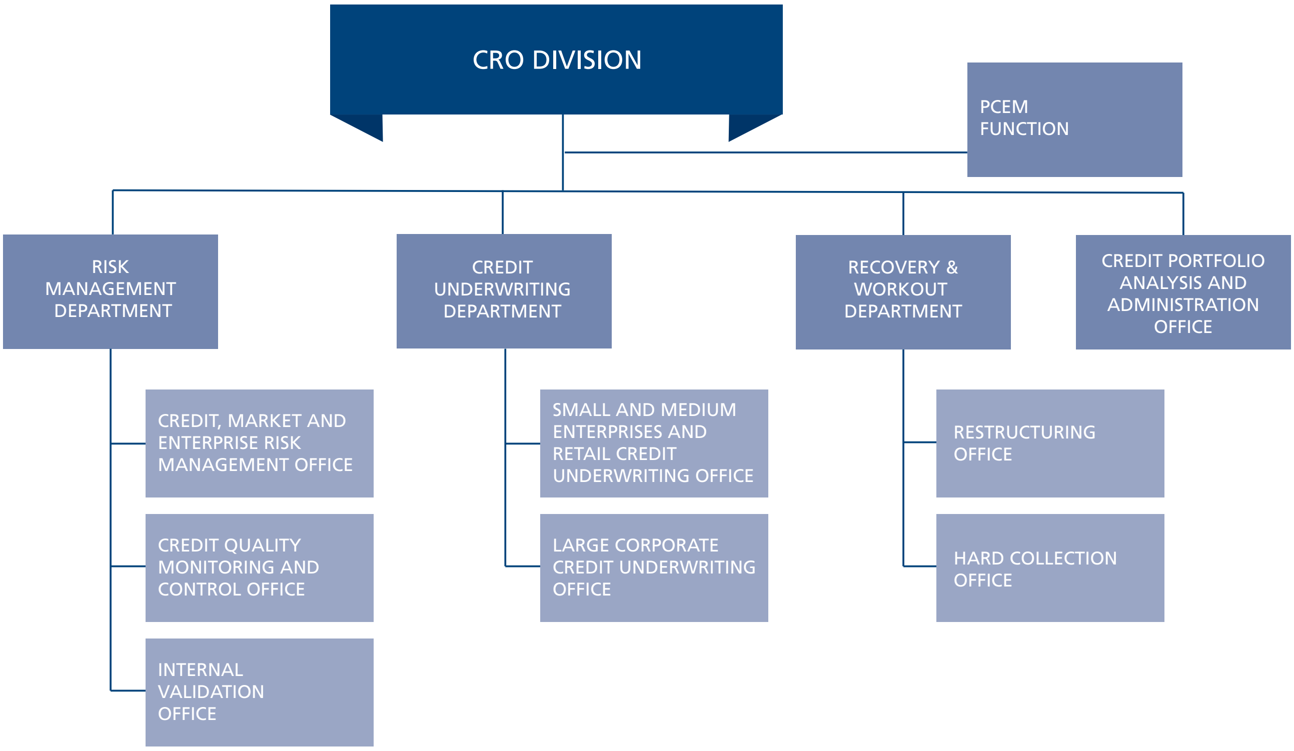
3.1.2. The organisational structure of Risk Division

The Risk Division (CRO area) is responsible for the risk management processes of the Bank. The person in charge of the Risk Division is a Member of the Management Board.

The reorganization of the Division continued in 2016 in order to enhance the control system of credit risk and achieve further alignment with the processes of the Parent Bank. For these purposes have been accomplished:

- A separation between Credit and Risk area, by assigning the principal Risk Management responsibilities within the Risk Management area,
- Extension of duties of the Loan Administration office within Credit area, by establishing the Credit Portfolio Analysis and Administration office, which is in charge of performing wider range of first level credit controls,
- Setting up of the Credit Quality Monitoring and Control office within Risk Management area, responsible for second level credit control and monitoring.

The organisation chart of the Risk Division:



The roles of organisational units within the Risk Division

Under the **Risk Management Department** are organized three offices, which have specific responsibilities related to second level risk control activities:

- **Credit market and enterprise risk management office** is responsible for risk policies, risk methodologies and reporting on risk exposures. In addition the Office monitors internal risk limits and external regulatory constraints, including the minimum capital adequacy ratios.
- **Credit Quality Monitoring and Control Office** is performing second level controls and monitoring activities over the credit portfolio, in terms of quality, composition and considerable changes.
- **The Validation Office** is in charge of evaluating the compliance of the internal systems of risk measurement and management with the regulatory requirements and their alignment with ISP Group guidelines. The Validation Office is responsible for the evaluation of the internal systems of all risk profiles (to be used for both regulatory and internal management purposes) in all the phases of the internal systems lifecycle, also supporting the Supervisory Authorities in their review activities.

  With specific regard to the credit risk, the role of Validation Office is to evaluate the adequacy and suitability of the internal rating systems, from both a design point of view (analysis of the methodological choices with regard to the regulatory requirements and internal and external best practices) and a performance point of view (back-testing analysis and periodical model monitoring). The validation analysis consists also of independent re-performance of the rating and development of alternative methodologies to be used as a benchmark.

Proactive credit exposure management contributes to the implementation of an early warning system, designed to activate the necessary measures against the identified clients by defining and agreeing with business functions the most proper action plans.

The Credit Underwriting Department analyses and approves loans and credit facilities to individual borrowers. There are two offices that operate within the framework of the Department: Small, Medium Enterprises and Retail Credit Underwriting Office and the Large Corporate Credit Underwriting Office.

The Recovery and Workout Department analyses and approves credit proposals for non-performing clients, participates in loan restructuring and in designing other measures in relation to borrowers with positive recovery perspective (going concern business) as much as in relation to obligors in legal enforcement status (gone concern business), seeking for the loss reduction and efficient recovery.

Credit portfolio analysis and administration office performs administrative controls in credit processes in order to verify the completeness of loan documentation before disbursement and performs credit portfolio analysis aimed at identifying negative trends and/or potential issues in the process, requiring further investigations by competent structures.

3.2 CAPITAL ADEQUACY AND OWN FUNDS (CAPITAL) MANAGEMENT

The Bank's capital includes common equity (mainly paid up capital and retained earnings) and eligible capital instruments, which have similar loss absorption characteristics as common shares. The function of the capital is the absorption of potential losses and as such protects depositors' savings.

The Bank meets the minimum capital requirement, as requested by the EU Regulation on prudential requirements for credit institutions (Capital Requirements Regulation or CRR). The CRR prescribes the minimum capital requirement, which is calculated according to the binding rules for the determination of risk- weighted assets. In addition, the CRR defines the general guidelines on the self-directed internal assessment of risk and capital requirement (Internal capital adequacy assessment process or ICAAP).

3.2.1 Compliance with the regulatory capital requirement

The regulatory capital requirement is calculated in line with CRR Regulation and is determined as a ratio between the Bank's capital and risk-weighted assets. Capital requirements have to be set aside for credit, market and operational risk. Banks have to meet the CET1 minimum capital requirement of 4.5% or higher, and the minimum own funds requirement of 8%. The Bank's capital is entirely composed of the Common Equity Tier 1 capital, which as at 30 December 2016 amounted to 257.17 million euros, whereas the CET1 ratio was 17.40%. The ratio was above the minimum capital requirement, as well as above the minimum ratio as defined by the supervisory review process (SREP) evaluation of Pillar II, which is based on a wider assessment of capital requirement of the Bank (ICAAP).

The Bank maintains the minimum capital adequacy and the minimum amount of capital by regularly reporting the capital position to the highest governance bodies and by providing annual and strategic capital planning. A capital growth corresponding to the increase of risk capital activities was provided with proper retention of profits within the capital reserves.

(in thousands of euros)

Capital adequacy as at 31 December 2016	Balance sheet/ Nominal amount		Risk weighted amount		Capital	
	2016	2015	2016	2015	2016	2015
Credit risk exposures of banking book						
Exposures to state and central bank	822,087	648,004	9,015	12,761	721	1,021
Exposures to local municipalities	54,771	60,873	10,894	12,134	872	971
Exposures to public sector	8,743	7,767	2,547	5,026	204	402
Exposures to development banks	538	1,415	-	-	-	-
Exposures to institutions	139,045	333,537	29,129	69,715	2,330	5,577
Exposures to enterprises	650,428	557,819	553,647	473,332	44,292	37,867
Exposures to equity	3,878	11,566	3,878	11,566	310	925
Exposures to retail banking	896,296	882,822	555,175	525,190	44,414	42,015
Past due exposures	89,641	130,893	101,777	149,517	8,142	11,961
Exposures to highly risk exposures	2	2	2	1	-	-
Exposures to investments funds	49,331	45,779	40,088	35,801	3,207	2,864
Exposures to other assets	65,619	64,904	49,505	49,284	3,960	3,943
Total	**2,780,379**	**2,745,381**	**1,355,657**	**1,344,327**	**108,452**	**107,546**
Credit risk weighted assets			1,355,657	1,344,327	108,452	107,546
Market risk weighted assets			965	1,315	77	105
Operational risk weighted assets			121,502	122,743	9,720	9,819
Total risk weighted assets			**1,478,124**	**1,468,385**	**118,249**	**117,018**
Regulatory capital						
Share capital			22,173	22,173		
Share premium			7,499	7,499		
Treasury shares			(49)	(49)		
Legal reserves			15,260	14,248		
Statutory reserves			214,053	213,357		
Treasury shares fund reserves			49	49		
Retained earnings due to transition to IFRS			6,009	6,009		
Accumulated other comprehensive income			5,859	10,452		
Less intangible assets			(4,068)	(4,471)		
Other transitional adjustments						
Unrealised gains/losses on government bonds			(5,584)	(7,725)		
Unrealised gains/losses on other shares			(339)	(2,018)		
Deferred tax assets that rely on future profitability and do not arise from temporary differences			-	(552)		
Requirements from prudent valuation of debt securities			(175)	-		
Recognised impairments for credit risk during the year			(3,513)	-		
Total qualifying Tier 1 capital			**257,174**	**258,972**		
Total qualifying Tier 2 capital			**-**	**-**		
Total regulatory capital			**257,174**	**258,972**		
Capital Adequacy ratio (%)			**17.40**	**17.64**		

3.2.2 Internal capital adequacy assessment (ICAAP)

The Internal Capital Adequacy Assessment Process (ICAAP) is governed by the Bank of Slovenia regulation on internal governance, governance bodies and bank ICAAP. The Bank performs the process also in line with the guidelines issued by the parent company, since the Bank ICAAP is included in the consolidated process at the parent group level. The purpose of ICAAP is to complement the regulatory minimum capital requirements with a comprehensive handling of all risks to which the Bank is exposed.

The ICAAP results are evaluated by the Bank supervision (the supervision is performed by the joint team of the ECB and the Bank of Slovenia) as part of the SREP activity and serving as a basis for the assessment of the capital requirements for the Bank.

The ICAAP process for the Bank is based on homogenous methodology of the parent company, taking into account specific peculiarities of the Bank and local regulation. The capital requirements methodology shows the results of a 99.9% confidence level and 1 year investment horizon.

The internally assessed capital sources (available financial resources), which defines the capacity to assume risk, comprises the regulatory capital and current profit, which will be distributed to Bank's capital reserves. During 2016, the Bank maintained an adequate amount of Available financial resources in terms of internally defined target capital ratio, as well as the requirements of the banking supervisor, as a result of the SREP assessment.

Internally established target level of the Available Financial Resources is established at 115% of capital requirements without stress scenarios. As at 31 December 2016, the available financial resources in relation to capital requirements without stress scenarios stood at 162.8%.

Internal assessment of capital requirement was carried out for all risks, which the Bank according to internal criteria classified as important risks:

Credit risk is the risk that the counterparty will not be able to repay financial obligations. Internally assessed capital requirement equals the amount of the regulatory capital requirement less the capital requirements for equity investments, which are assessed as a distinct risk category.

Market risk is the risk of loss on trading activities due to change of market value. Internal capital is equal to the regulatory capital requirement.

Operational risk is the risk arising from the conduct of people, inadequate processes and systems or external events. It includes legal risk. Internal capital is equal to regulatory capital requirement for operational risk.

Banking book financial risks includes equity risk and interest rate risk, and liquidity risk.

Banking book equity risk covers the risk of equity investments, which are not for strategic purpose and the Bank acquired through the repossession of credit collateral. Capital requirement is calculated according to IRB method with simple weighting.

Interest rate risk in the banking book is defined as the risk of interest rate change having adverse impact on net interest income from non-trading activities. Capital requirement is calculated with a historical simulation on 5-year interest rate historical data. A simulation of yields curves represents interest rates shock, based on which is obtained a combined impact on net interest income and cash-flow net present value at given statistical confidence level.

Strategic risk is the risk of decline in profit margin due to change in the business environment, wrong business decisions and insufficient reaction to changes in the business environment. The internal capital is set in relation to the risk of disadvantageous evolvement of every major component of the business margin on the operating revenues and cost, estimate with a parametric VaR.

Credit concentration risk pays regards to single-name concentration in the credit portfolio and concentration risk by industries. The modified BoS methodology is used for single-name concentration calculation adjusted according to Parent Company guideline.

AFS Fixed income investments market risk: under this risk category the Bank takes in consideration the market risk of Banking book investments, measured at fair value, specifically referring to fixed income portfolio. To calculate the economic capital, the average of daily AFS Bond portfolio VaR, with 99% confidence level is used.

Real estate risk is represented by the risk of reduction of prices of real estate property, repossessed by the Bank with the collateral execution during the credit recovery activity. Economic capital is estimated is estimated with the Maximum Potential Loss (MPL), using the maximum annual historical negative variation in real estate prices, recorded over the entire observation period (1988-2016).

Internal capital under stress scenarios

The internal assessment of capital requirements evaluated on the baseline scenario is afterwards assessed also under stressed conditions. Stress-test takes into consideration a prospective evolution of position over one year and stressing conditions.

The relevance and necessity to compute capital requirements according to stress scenarios is verified for each of the identified material risk under baseline scenario. The stress test shocks are evaluated for their impact on the amount of required capital and on the reduction of Available financial resources:

- Shock on credit risk takes in the consideration a reduction of GDP by 2,5 percentage points, compared to the UMAR forecasted (Institute of macroeconomic analysis and development) figure.
- As for the operational risk, the bases for the calculation of stress test on internal capital are loss events registered in the last 10 years. Impact of stress test on internal capital is calculated as a sum of the largest differences between worst yearly losses and the yearly average for each event type. Stress test on AFR on the other hand is calculated as the average of the 5 most relevant losses recorded in the last 5 years.
- Additional capital requirement for the Banking book interest rate risk is estimated applying a 200 bps parallel shift. In addition is evaluated the impact of adverse interest rate change on Available Financial Resources.
- For equity risk is estimated the impact of a 25% drop for the domestic Stock-exchange index on Available financial resources, through the fair value revaluation of equity investments acquired by the Bank with repossession of credit collaterals.
- The impact due to the strategic risk is calculated by envisioning adverse change of GDP growth and interest rate on the Available financial resources. A higher Economic capital is estimated taking into account higher variability of operative earnings, aligning it with historical peak, taking into account potential additional pressure on interest margin due to low interest rates.

Internally assessed capital requirements as at 31 December 2016 and as at 31 December 2015:

(in millions of euros)

Risk	31. 12. 2016	31. 12. 2015
Credit Risk	106.16	107.06
Market Risk	0.08	0.11
Operational Risk	9.72	9.82
Banking Book Risk	9.50	10.86
- Interest Rate Risk	8.48	9.19
- Equity Risk	1.02	1.67
Strategic Risk	6.58	8.40
Concentration of credit risk	16.99	2.14
AFS Fixed income investments market risk	5.75	-
Real Estate Risk	3.21	-
Stress test scenario	21.50	29.55
Total capital charges	**179.49**	**167.94**
Available financial resources	**257.17**	**259.67**

The add-on for stress scenario, decreased from EUR 29.55 mln in 2015 to EUR 21.49 mln in 2016. The biggest change is the exclusion of the stress test for market risk for AFS bonds portfolio, which had the second biggest contribution after credit risk in the previous year. This risk component was included under risk categories for capital needs as AFS fixed income investment market risk.

3.2.3 Risk Appetite Framework Limits

With the Risk Appetite Framework (RAF) Limits have been established a system of risk metrics that represents risk amounts the Bank is willing to assume. The RAF limits represent the highest level of aggregate risk representation with break down to capital adequacy, liquidity and credit concentration limits. Alongside the limits the Risk Appetite Framework establishes also controls and procedures in case of limit breach and the roles regarding the definition and approval of RAF limits. The RAF limits define also the target amount of Available financial resources (internally assessed available capital sources) through the target AFR/ECAP ratio (Available Financial Resources/ICAAP capital charges excluding stress test).

3.3 CREDIT RISK

Credit risk is the risk of financial loss arising from a debtor's failure to repay its financial obligations. Credit risk is, by scope and business strategic orientation, the most important risk for the Bank.

The credit risk is associated with financial assets measured at amortised cost (loans and other claims). For such assets the credit risk is evaluated with accurate credit risk analysis and corresponding credit classification of the borrower. Credit risk of derivative contracts is measured at replacement cost. The replacement cost is made up of the positive value of the deal, which represents a positive difference between the settlement price and the contractual price of the instrument, increased for the add-on, accommodating for a potential increase of positive value. The replacement cost is made up of the positive value of the deal, which represents a positive difference between the settlement price and the contractual price of the instrument, increased for the add-on, accommodating for a potential increase of positive value.

Banka Koper's credit risk related portfolio at the end December 2016 amounted to EUR 2.473 million of which 93% is classified as performing. Credit risk portfolio includes all asset and off-balance sheet items, which are subject to credit risk according to the Bank of Slovenia methodology.

Banka Koper's credit risk related portfolio as at 31 December 2016

(in thousands of euros)

Counterparties	Total risk portfolio	Total credit risk related portfolio	Share in %	Performing	Share in %	Non performing	Share in %	Impairment losses on performing portfolio	Coverage rate of performing portfolio	Impairment losses on non performing portfolio	Coverage rate of non performing portfolio
1	2	3	4	5	6	7	8	9	10=9/5	11	12=11/7
Central bank and government bodies	527,735	205,964	8%	205,964	9%	-	0%	43	0%	-	0%
Corporate entities	1,487,050	1,465,567	59%	1,299,697	57%	165,870	91%	17,686	1%	84,067	51%
Banks	166,035	138,102	6 %	138,102	6 %	-	0%	32	0%	-	0%
Private individuals	663,619	663,619	27%	648,040	28%	15,579	9%	1,050	0%	7,553	48%
Total	**2,844,439**	**2,473,252**	**100%**	**2,291,803**	**100%**	**181,449**	**100%**	**18,811**	**1%**	**91,620**	**50%**

Banka Koper's credit risk related portfolio as at 31 December 2015

(in thousands of euros)

Counterparties	Total risk portfolio	Total credit risk related portfolio	Share in %	Performing	Share in %	Non performing	Share in %	Impairment losses on performing portfolio	Coverage rate of performing portfolio	Impairment losses on non performing portfolio	Coverage rate of non performing portfolio
1	2	3	4	5	6	7	8	9	10=9/5	11	12=11/7
Central bank and government bodies	436,348	148,019	6%	148,019	7%	-	0%	-	0%	-	0%
Corporate entities	1,409,583	1,381,106	55%	1,136,252	51%	244,854	94%	18,215	2%	121,931	50%
Banks	357,069	326,983	13%	326,983	14%	-	0%	-	0%	-	0%
Private individuals	642,073	642,073	26%	626,631	28%	15,442	6%	1,947	0%	6,645	43%
Total	**2,845,073**	**2,498,181**	**100%**	**2,237,885**	**100%**	**260,296**	**100%**	**20,162**	**1%**	**128,576**	**49%**

Analyses by type of collateral

(in thousands of euros)

	2016		2015	
	Net loans	Fair value of collateral	Net loans	Fair value of collateral
Real estate	478,589	1,557,240	472,878	1,515,032
Bank guarantees	44,983	60,933	19,997	21,791
Personal guarantees	235,665	634,857	226,226	648,780
Debt securities	12,750	36,150	22,255	47,658
Government guarantees	254,064	280,998	151,174	151,229
Other collateral	90,679	263,033	111,923	425,843
Deposits	2,134	4,422	2,247	4,655
Insurance company guarantees	105,167	126,303	109,184	128,458
Total collateralised net loans	**1,224,031**	**2,963,936**	**1,115,884**	**2,943,446**
Unsecured	402,342		366,798	
Total net loans to customers	**1,626,373**		**1,482,682**	

In general loans can be secured with one or more types of collateral. The Bank's decision when collateral is acceptable depends on the obligor's credit worthiness and the type, amount and maturity of lending facilities. The value of collateral is monitored and periodically revalued as its fair value changes. Securities and collective investment units are revalued weekly, whereas real estate and movable property collateral are revalued yearly.

Credit risk measurement

The Bank`s credit portfolio includes cash exposures, commitments to lend and off-balance sheet commitments. The credit exposures arising from derivative contracts are reported at replacement cost.

(in thousands of euros)

Maximum exposure to credit risk	2016	2015
Credit risk exposures relating to on-balance sheet assets are as follows:		
Loans to banks	89,516	160,140
Loans to non-bank customers:	1,626,373	1,482,682
- Loans to individuals:	533,984	510,393
- overdrafts	24,822	28,723
- credit cards	17,568	18,224
- term loans	100,758	98,630
- mortgages	382,986	355,143
- finance leases	7,850	9,673
- Loans to sole proprietors	51,825	56,920
- Loans to corporate entities	1,040,564	915,369
Advances	11,016	11,919
Available for sale financial assets:	340,111	307,908
- debt securities	340,111	307,908
Other assets	201,171	251,089
Credit risk exposures relating to off-balance sheet items are as follows:		
Guarantees	180,108	176,757
Credit commitments and other credit related liabilities	285,713	305,840
At 31 December	**2,734,008**	**2,696,335**

The maximum exposure to credit risk represents the worst case scenario of credit risk exposure to the Bank at 31 December 2016 and 2015, without taking into account any collateral held or other attached credit enhancements. For on-balance-sheet assets, the exposures set out above are based on net carrying amounts as reported in the statement of financial position.

Credit Classification

The Bank`s credit portfolio is classified in 5 basic credit risk categories in accordance with the classification rules of the Bank of Slovenia. Exposures to obligors with the highest credit worthiness or exposures guaranteed by the state are classified in the A category, whereas the exposures to obligors with the lowest credit worthiness are classified in the E category. The credit ranking is supported by the probability that the obligor will not be able to repay the obligations. The credit assessment takes into account the financial standing of the obligor, the cash-flow availability to service the debt and payment regularity record. The performing obligors are classified into credit grades A, B or C.

Obligors with internal rating calculated by statistical model are in parallel classified in 13 credit categories.

The bank has been developing internal ratings for all major obligor segments. The internal rating system is based on a statistical analysis of the default probability assigned to each obligor rating grade. Currently, internal ratings are assigned to Corporate and Small business obligors, while for the other segments the internal rating models are in development stage. The statistical models are designed to contain the debtor's financial data, behavioural data and qualitative information, which jointly contributes to the final obligor's credit classification. The classification attribution process is supported by the system, which has required controls that are driving the logical process of the classification attribution.

The obligor's classification is compliant with the European Banking Authority requirements, which has established rules for the classification of exposures to performing or non-performing categories. The non-performing obligors are further broken-down into the following categories: past due, unlikely to pay and doubtful. The work-out strategy for non-performing obligors depends on whether the Bank evaluates the borrower as going concern or gone concern, with the later expecting that the financial difficulties cannot be resolved.

Banka Koper's classification	2016		2015	
	Loans and advances (%)	Coverage with impairments (%)	Loans and advances (%)	Coverage with impairments (%)
Performing	87	0.5	85	0.7
Watch list	5	8.3	4	7.6
Substandard	3	37.4	5	31.3
Doubtful	5	57.4	6	65.9
	100	**5.0**	**100**	**6.5**

Impairment provisions for credit risk

The amount of impairment provisions for credit risk is commensurate with the credit standing of the borrower and collateral received in pledge. Provisions are calculated using collective or individual approach. Credit risk losses are calculated individually for obligors, whose total exposure exceeds 250,000 euros and are classified as non-performing. The Individual approach is carried out with the estimation of all expected cash-flows for each obligor individually that can be recovered from the obligor's own assets or earnings and through the execution of collateral. The expected cash-flow has to be discounted using the original contract's interest rate.

Under the collective provisioning methodology, provisions are calculated by estimating the expected loss as a result of a multiplication of the probability of default (PD rate), the expected loss given such default (LGD rate) and the expected exposure at the time of default (EAD). Loss estimation parameters are updated annually.

For the Corporate and Small business segment the probability of default is determined using the internal rating, whereas for other obligor segments the expected loss is estimated with calculation of annual migration rates between classification categories (Annual Default Rate). The estimation is done using the average of 5-year historical series.

Loss Given Default rates are estimated by groups of exposures of different obligors segments secured with the same type of collateral. The recovery rate is estimated using the ratio between the net present values of recoveries, less costs, and credit exposures at default (the work-out method). The estimation is made based on 6-year historical series of recovery data.

Loans that are considered genuinely unrecoverable are written off after all available legal actions have been taken. In cases where the amount of impairment is excessive due to improvement in the economic position of the obligor, the previously recognised impairment is reversed by debiting the loan losses adjustment account and crediting the income statement.

Large exposures

In order to limit the risk of large exposure, the Bank monitors the single-name credit concentration risk. The largest allowed exposure to a single borrower and connected entities is limited by CRR Regulation and should not exceed 25 per cent of the Bank's regulatory capital. In case of exposure to banks or banking groups the maximum allowed exposure is EUR 150 million.

Financial instrument`s breakdown by country risk

(in thousands of euros)

As at 31 December 2016	Slovenia	EU	*Of which Italy*	Other Europe	Rest of world	Total
Cash, cash balances at Central Banks and other demand deposits at banks	153,558	33,687	*31,359*	146	5,452	**192,843**
Financial assets held for trading:	-	64	*64*	-	-	**64**
- derivative financial instruments	-	64	*64*	-	-	**64**
Financial assets designated at fair value through profit or loss	-	136	*136*	-	-	**136**
Available for sale financial assets	254,567	98,899	*98,869*	-	1,149	**354,615**
Loans and receivables:	1,577,924	93,622	*82,254*	31,252	24,107	**1,726,905**
- loans to banks	3,815	85,701	*77,717*	-	-	**89,516**
- loans to non-bank customers	1,567,165	6,608	*4,448*	31,189	21,411	**1,626,373**
- advances	6,944	1,313	*89*	63	2,696	**11,016**
Derivatives – hedge accounting	-	913	-	-	-	**913**
Contingent liabilities and commitments	**450,771**	**5,350**	***3,647***	**1,116**	**29**	**457,266**
Total exposures	**2,436,820**	**232,671**	***216,329***	**32,514**	**30,737**	**2,732,742**

(in thousands of euros)

As at 31 December 2015	Slovenia	EU	*Of which Italy*	Other Europe	Rest of world	Total
Cash, cash balances at Central Banks and other demand deposits at banks	93,244	138,184	*122,174*	573	2,239	**234,240**
Financial assets held for trading:	-	91	*91*	-	-	**91**
- derivative financial instruments	-	91	*91*	-	-	**91**
Financial assets designated at fair value through profit or loss	-	222	*222*	-	-	**222**
Available for sale financial assets	237,646	92,442	*81,632*	-	-	**330,088**
Loans and receivables:	1,426,529	163,584	*144,993*	36,447	28,181	**1,654,741**
- loans to banks	3,394	156,746	*141,746*	-	-	**160,140**
- loans to non-bank customers	1,414,626	5,880	*3,204*	36,441	25,735	**1,482,682**
- advances	8,509	958	*43*	6	2,446	**11,919**
Derivatives – hedge accounting	-	21	-	-	-	**21**
Contingent liabilities and commitments	**451,108**	**23,463**	***18,647***	**1,282**	**19**	**475,872**
Total exposures	**2,208,527**	**418,007**	***367,759***	**38,302**	**30,439**	**2,695,275**

3.4 ANALYSIS OF PAST DUE FINANCIAL INSTRUMENTS

Past due financial instruments relate only to loans and advances portfolio, meanwhile other financial instrument portfolios do not record delays.

Loans and advances are summarised as follows:

Loans and advances by maturity (past due)

(in thousands of euros)

	31 December 2016		31 December 2015	
	Loans and advances to customers	Loans and advances to banks	Loans and advances to customers	Loans and advances to banks
Neither past due nor impaired	1,551,905	89,532	1,363,305	160,140
Past due but not impaired	2,991	-	5,866	-
Impaired	175,848	-	254,393	-
Gross	**1,730,744**	**89,532**	**1,623,564**	**160,140**
Impairment losses on loans and advances	(104,371)	(16)	(140,882)	-
Net	**1,626,373**	**89,516**	**1,482,682**	**160,140**

Loans and advances to customers by maturity and portfolio quality

(in thousands of euros)

31 December 2016	Individuals							
	Overdrafts	Credit Cards	Term loans	Mortgages	Finance leases	Sole proprietors	Corporate entities	Total loans and advances to customers
Neither past due nor impaired	24,224	16,739	99,200	378,383	7,097	48,216	978,046	1,551,905
Not past due but impaired	72	13	689	3,190	270	1,311	57,722	63,267
Past due but not impaired	170	662	162	207	64	215	1,511	2,991
Past due and impaired	1,372	868	2,729	5,349	706	9,188	92,369	112,581
Gross	**25,838**	**18,282**	**102,780**	**387,129**	**8,137**	**58,930**	**1,129,648**	**1,730,744**
Impairment losses on loans and advances	(1,016)	(714)	(2,022)	(4,143)	(287)	(7,105)	(89,084)	(104,371)
Net	**24,822**	**17,568**	**100,758**	**382,986**	**7,850**	**51,825**	**1,040,564**	**1,626,373**

Loans under "not past due but impaired" relate mainly to restructured loans.

(in thousands of euros)

31 December 2015	Individuals					Sole proprietors	Corporate entities	Total loans and advances to customers
	Overdrafts	Credit Cards	Term loans	Mortgages	Finance leases			
Neither past due nor impaired	28,028	17,299	96,652	350,574	8,475	52,336	809,941	1,363,305
Not past due but impaired	71	8	868	2,895	860	2,332	74,277	81,311
Past due but not impaired	312	734	198	195	73	268	4,086	5,866
Past due and impaired	1,266	952	2,469	5,052	695	9,052	153,596	173,082
Gross	**29,677**	**18,993**	**100,187**	**358,716**	**10,103**	**63,988**	**1,041,900**	**1,623,564**
Impairment losses on loans and advances	(954)	(769)	(1,557)	(3,573)	(430)	(7,068)	(126,531)	(140,882)
Net	**28,723**	**18,224**	**98,630**	**355,143**	**9,673**	**56,920**	**915,369**	**1,482,682**

Ageing of past due loans and advances to customers by type of customer, product and portfolio quality

(in thousands of euros)

31 December 2016	Individuals										Total individuals
	Overdrafts		Credit cards		Term loans		Mortgages		Finance leases		
	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	
Past due up to 30 days	135	7	566	7	124	61	159	134	49	8	1,250
Past due 30 - 60 days	25	1	79	12	16	57	28	21	13	8	260
Past due 60 - 90 days	8	3	17	7	22	10	19	127	2	8	223
Past due over 90 days	2	1,361	-	842	-	2,601	1	5,067	-	682	10,556
Total	**170**	**1,372**	**662**	**868**	**162**	**2,729**	**207**	**5,349**	**64**	**706**	**12,289**

31 December 2016	Sole proprietors		Corporate entities		Total
	Not impaired	Impaired	Not impaired	Impaired	
Past due up to 30 days	144	32	1,266	338	1,780
Past due 30 - 60 days	68	95	170	602	935
Past due 60 - 90 days	3	79	75	86	243
Past due over 90 days	-	8,982	-	91,343	100,325
Total	**215**	**9,188**	**1,511**	**92,369**	**103,283**

Decrease of past due loans and advances in 2016 is mainly due to write-offs. Write-offs of non-performing loans amounted to EUR 57,243 thousand (2015: EUR 23,762 thousand).

Ageing of past due loans and advances to customers by type of customer, product and portfolio quality

(in thousands of euros)

31 December 2015	Individuals										Total individuals
	Overdrafts		Credit cards		Term loans		Mortgages		Finance leases		
	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	
Past due up to 30 days	157	7	617	17	174	41	162	169	57	16	1,417
Past due 30 - 60 days	75	2	92	10	20	36	21	113	14	15	398
Past due 60 - 90 days	79	17	24	12	4	15	8	106	2	16	283
Past due over 90 days	1	1,240	1	913	-	2,377	4	4,664	-	648	9,848
Total	**312**	**1,266**	**734**	**952**	**198**	**2,469**	**195**	**5,052**	**73**	**695**	**11,946**

31 December 2015	Sole proprietors		Corporate entities		Total
	Not impaired	Impaired	Not impaired	Impaired	
Past due up to 30 days	177	42	3,444	1,135	4,798
Past due 30 - 60 days	76	135	448	858	1,517
Past due 60 - 90 days	12	48	181	159	400
Past due over 90 days	3	8,827	13	151,444	160,287
Total	**268**	**9,052**	**4,086**	**153,596**	**167,002**

The breakdown of the gross amount of individually impaired loans and advances by class, along with the fair value of related collateral held by the Bank as security, is as follows:

Loans and advances individually impaired

(in thousands of euros)

31 December 2016	Individuals	Sole proprietors	Corporate entities	Total
Individually impaired loans	2,746	1,468	127,762	131,976
Fair value of collateral	3,494	1,936	171,363	176,793

31 December 2015	Individuals	Sole proprietors	Corporate entities	Total
Individually impaired loans	-	7,185	220,171	227,356
Fair value of collateral	-	14,453	303,803	318,256

In 2016, the Bank received EUR 9,726 thousand from the sale of pledged collateral.

3.5 LIQUIDITY RISK

Liquidity risk is defined as the risk of not being able to meet payment obligations as they fall due, due to difficulties to finance liquidity needs, or convert marketable assets into cash, including potential losses incurred due to forced trades. In order to manage liquidity risk, the Bank monitors liquidity ratio levels and mandatory reserves on a daily basis in order to maintain adequate liquidity position.

The minimum liquidity to be maintained by banks is defined by the Bank of Slovenia Regulation on the minimum requirements for ensuring an adequate liquidity position (Ur. l. RS, št. 50/15), establishing a minimum liquidity ratio for assets and liabilities with maturity up to one month.

The liquidity position of the Bank is monitored with two additional ratios, the LCR (Liquidity Coverage Ratio) and NSFR (Net Stable Funding Ratio). The ratios have been introduced globally as principal liquidity measures necessary to ensure a minimum short-term liquidity as well long-term balanced funding of banks. Beside the mentioned indicators, the Bank as well calculates the so-called 'Stress LCR", which is meant for monitoring the Bank's liquidity position in uncertain (stress) situation. . It measures the LCR over a 3 month period. In 2016 all indicators are calculated in accordance with the Delegated Act regulation (2015/61), which came into force in 2015, instead of Capital Requirements Regulation (575/2013). LCR and NSFR indicators are regularly reported to ALCO and Audit Committee.

Liquidity ratios

	31.12.2016	31.12.2015	31.12.2014
LCR	246%	329%	357%
NSFR	139%	139%	134%

The LCR and NSFR ratios through the past period were stable, showing no significant movement and compliant with the regulatory limit. In 2016 Banka Koper adopted a new Liquidity policy in line with the new Group guidelines on liquidity risk, where the new internal limit for LCR was established at 90%. The regulatory limit in force in 2016 was 70% for LCR and 90% for NSFR. The LCR ratio as of 31 December 2016 decreased compared to previous years, due to lower amount of expected cash inflows with residual maturity below 1 month, which oscillate in the short term based on Treasury operations on money markets (placement on interbank market or with central bank facilities), while in the medium term the liquidity position remains stable.

The Treasury and ALM Department manages at the operating level the liquidity with daily cash-flow planning and maintains an adequate amount of eligible assets as collateral necessary for refinancing with the ECB.
The measures aimed at managing a liquidity crisis are defined with the Contingent Liquidity Plan, establishing early warning indicators and roles and actions to be considered in adverse financial circumstances.

Maturities of assets and liabilities - Non-derivative cash flows by Expected maturities

(in thousands of euros)

As at 31 December 2016			Expected maturity				
	Carrying amount	Gross nominal Inflow/(outflow)	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
ASSETS							
Cash, cash balances at Central Banks and other demand deposits at banks	192,843	192,843	175,394	-	-	-	17,449
Financial assets designated at fair value through profit or loss	136	136	-	-	-	136	-
Available for sale financial assets	354,615	354,615	1,354	11,116	66,379	186,490	89,276
Loans and receivables:	1,726,905	1,743,058	143,195	130,637	222,326	692,494	554,406
- loans to banks	89,516	89,516	19,927	67,989	1,600	-	-
- loans to non-bank customers	1,626,373	1,642,526	118,019	56,881	220,726	692,494	554,406
- advances	11,016	11,016	5,249	5,767	-	-	-
Total assets	**2,274,499**	**2,290,652**	**319,943**	**141,753**	**288,705**	**879,120**	**661,131**
LIABILITIES							
Financial liabilities measured at amortised cost:	2,017,524	2,017,524	1,500,158	125,517	268,191	104,311	19,347
- deposits from banks and central banks	62,700	62,700	1,037	9,998	42,332	9,333	-
- deposits from non-bank customers	1,839,935	1,839,935	1,476,759	108,070	217,328	36,200	1,578
- loans from banks and central banks	87,747	87,747	1,960	1,499	7,741	58,778	17,769
- loans from non-bank customers	28	28	3	14	11	-	-
- other financial liabilities	27,114	27,114	20,399	5,936	779	-	-
Total assets	**2,017,524**	**2,017,524**	**1,500,158**	**125,517**	**268,191**	**104,311**	**19,347**
Net liquidity gap	**256,975**	**273,128**	**(1,180,215)**	**16,236**	**20,514**	**774,809**	**641,784**

As at 31 December 2015			Expected maturity				
	Carrying amount	Gross nominal Inflow/(outflow)	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
Total assets	2,219,291	2,234,725	395,193	172,730	344,017	850,664	472,121
Total liabilities	1,971,643	(1,971,643)	(1,314,742)	(179,930)	(299,491)	(129,656)	(47,824)
Net liquidity gap	**247,648**	**263,082**	**(919,549)**	**(7,200)**	**44,526**	**721,008**	**424,297**

The negative net liquidity gap in the 1 month time bucket should be viewed with additional consideration of specific liquidity profile of some balance sheet items, particularly demand deposits, which balances during 2016 increased significantly. Although demand deposits can be withdrawn at any time, they are considered (for liquidity management purposes) to be largely stable. This is demonstrated by the LCR treatment of demand deposits, whereby the run-off factor is 5%, representing the percentage of demand deposits deemed volatile in one month horizon. Moreover, on the assets side the available for sale financial assets include ECB eligible bonds, which are regarded as liquidity reserves entering in the 1 month maturity bucket. The stable part of demand deposits and ECB eligible bonds counterbalance the 1 month net liquidity gap and changes it to positive net liquidity position according to LCR liquidity indicator.

Maturities of assets and liabilities Derivative cash flows by expected maturity

(in thousands of euros)

As at 31 December 2016	Carrying amount	Nominal Inflow/(outflow)	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
			Expected maturity				
DERIVATIVE ASSETS							
Derivatives held for trading:							
Interest rate cap	**64**	**(143)**	**-**	**-**	**27**	**498**	**(668)**
Inflow		76,440	-	-	101	15,068	61,271
Outflow		(76,583)	-	-	(74)	(14,570)	(61,939)
Total	**64**	**(143)**	**-**	**-**	**27**	**498**	**(668)**
DERIVATIVE LIABILITIES							
Derivatives held for trading:							
Interest rate cap	**-**	**2**	**-**	**-**	**(4)**	**(3)**	**9**
Inflow		969	-	-	10	963	23
Outflow		(967)	-	-	(14)	(939)	(14)
Total	**-**	**2**	**-**	**-**	**(4)**	**(3)**	**9**
Net liquidity gap		**(145)**	**-**	**-**	**31**	**501**	**(677)**

As at 31 December 2015	Carrying amount	Nominal Inflow/(outflow)	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
			Expected maturity				
Total derivative held for trading assets	91	(64)	76	-	11	657	(808)
Total derivative held for trading liabilities	1	(72)	(76)	-	(1)	(33)	38
Net liquidity gap		**8**	**152**	**-**	**12**	**690**	**(846)**

Maturities of assets and liabilities Derivative cash flows by expected maturity

(in thousands of euros)

As at 31 December 2016	Carrying amount	Nominal Inflow/(outflow)	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
			Expected maturity				
DERIVATIVE ASSETS							
Derivatives held for hedge accounting:							
IRS	**913**	**(1,193)**	**38**	**4**	**48**	**(285)**	**(988)**
Inflow		3,016	38	215	836	1,490	437
Outflow		(4,209)	-	(211)	(788)	(1,775)	(1,435)
Total	**913**	**(1,193)**	**38**	**4**	**48**	**(285)**	**(998)**
DERIVATIVE LIABILITIES							
Derivatives held for hedge accounting:							
IRS	**1,402**	**1,468**	**398**	**169**	**384**	**4,217**	**(3,700)**
Inflow		14,931	501	261	970	6,689	6,510
Outflow		(13,463)	(103)	(92)	(586)	(2,472)	(10,210)
Total	**1,402**	**1,468**	**398**	**169**	**384**	**4,217**	**(3,700)**
Net liquidity gap		**(2,661)**	**(360)**	**(165)**	**(336)**	**(4,502)**	**2,702**

As at 31 December 2015	Carrying amount	Nominal Inflow/(outflow)	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
			Expected maturity				
Total derivative held for hedge accounting assets	21	22	-	91	(126)	57	-
Total derivative held for hedge accounting liabilities	66	(67)	-	(116)	63	(14)	-
Net liquidity gap	**-**	**89**	**-**	**207**	**(189)**	**71**	**-**

Cash flows of interest rate caps, interest options and interest rate swaps represent fairly the difference between contractual price and market price of derivatives.
The increase of cash-flows from derivatives in 2016 is a result of new IRS contracts made with the aim of providing interest rate hedge on loans extended with fixed contractual interest rate.

Expected maturities of off-balance sheet items

(in thousands of euros)

As at 31 December 2016	Expected maturity			
	No later than 1 year	1-5 years	Over 5 years	Total
Documentary and commercial letters of credit	159	-	-	159
Guarantees	121,792	35,728	20,158	177,678
Credit commitments	252,266	30,031	-	282,297
Total	**374,217**	**65,759**	**20,158**	**460,134**

As at 31 December 2015	Expected maturity			
	No later than 1 year	1-5 years	Over 5 years	Total
Total	**401,807**	**57,447**	**21,025**	**480,279**

3.6 BANKING BOOK EQUITY RISK

Equity risk is defined as the risk of unexpected losses arising from positions in available-for sale equity investments (shares or equity participations).
The Bank acquired these equity investments mainly with the repossession of financial collaterals arising from lending activity. These investments are managed pursuing the target of disposal in order to recover the relative credit exposures.

3.7 MARKET RISK

Market risk mainly arises from trading activities. The Bank only performs trading activities with the aim to respond to the demand of its customers and these activities mostly consist of buying and selling currency and derivative contracts.

The operational risk arising from trading activities are managed on the basis of a clear division between the front and back-office operations, which assures adequate controls and segregation of functions.

The Bank has established the market risk limits on Fixed income VaR indicator and FX VaR indicator and open position by currencies.

3.7.1 Derivative instruments

The Bank takes on derivative transactions only for the purpose of serving customers requests. Since the Bank is not willing to assume any financial risk embedded in derivative contracts (position risk or change in the fair value of a derivative due to change in the value of the underlying asset), each single transaction is fully hedged back-to-back by immediately executing an offsetting transaction with another bank. The Bank assumes only the counterparty risk in these transactions, i.e. risk of substituting the original contract with other counterparty. The counterparty credit risk for the purpose of internal credit risk monitoring is determined as an amount equal to replacement cost, which is calculated as the highest value between the positive fair value of the instrument and a percentage of the nominal amount equivalent to the counterparty credit risk. The credit counterparty risk percentage is determined with internal model developed by the Group and applied according to the type and maturity of derivative contract.

3.7.2 Currency Risk

When there is an open position in a particular currency, the Bank is exposed to currency risk. The open currency position in a particular foreign currency is the difference between assets and liabilities denominated in that currency. For the purpose of measuring currency risk, the Bank takes into account the overall position composed of assets and liabilities denominated in that currency, FX spot transactions and currency derivatives.

The Bank measures and monitors currency risk on a daily basis:

- as a notional open position for a particular currency, and
- as Value-at-Risk (VAR) indicator for the global currency position.

The Value-at-Risk is a statistical estimation of a maximum loss at the 99 per cent confidence level over a 1-day period. The Value-at-Risk measure is proportional to the currencies open position and to the exchange rate volatility.

The average utilisation of FX Var limit in 2016 was 10.22% and the average utilization of Fixed income Var limit was 41.82%.

Bank VAR by risk type

(in million of euros)

	12 months to 31 December 2016			12 months to 31 December 2015		
	Average	High[1]	Low[1]	Average	High[1]	Low[1]
Foreign exchange risk (trading and non-trading portfolio)	3	8	1	2	7	-
Bond risk (banking book)	708	1,082	335	582	885	400
Total VAR	**711**	**1,090**	**336**	**584**	**892**	**400**

[1] Highest and lowest 99% VaR calculated for one-day observation period for the 12-month period as indicated in the table.

Currency risk

(in thousands of euros)

As at 31 December 2016	EUR	USD	Other	Total
ASSETS				
Cash and balances with central banks and other demand deposits at banks	171,688	5,283	15,872	192,843
Financial assets held for trading:	64	-	-	64
- derivative financial instruments	64	-	-	64
Financial assets designated at fair value through profit or loss	136	-	-	136
Available for sale financial assets	308,393	46,222	-	354,615
Loans and receivables:	1,684,891	30,834	11,180	1,726,905
- loans to banks	73,553	9,985	5,978	89,516
- loans to non-bank customers	1,600,332	20,840	5,201	1,626,373
- advances	11,006	9	1	11,016
Derivatives – hedge accounting	664	249	-	913
Total assets	**2,165,836**	**82,588**	**27,052**	**2,275,476**
LIABILITIES				
Financial liabilities measured at amortised cost:	1,907,534	83,349	26,641	2,017,524
- deposits from banks and central banks	62,691	-	9	62,700
- deposits from non-bank customers	1,751,749	61,656	26,530	1,839,935
- loans from banks and central banks	66,854	20,893	-	87,747
- loans from non-bank customers	28	-	-	28
- other financial liabilities	26,212	800	102	27,114
Derivatives – hedge accounting	1,335	67	-	1,402
Total liabilities	**1,908,869**	**83,416**	**26,641**	**2,018,926**
Net balance sheet position	**256,967**	**(828)**	**411**	**256,550**
Part of contingent liabilities and commitments sensitive to currency risk	**279,568**	**3,112**	**30**	**282,710**

(in thousands of euros)

As at 31 December 2015	EUR	USD	Other	Total
Total assets	2,099,532	93,874	25,997	2,219,403
Total liabilities	1,848,887	96,645	26,178	1,971,710
Net balance sheet position	**250,645**	**(2,771)**	**(181)**	**247,693**
Part of contingent liabilities and commitments sensitive to currency risk	**289,612**	**14,395**	**1,384**	**305,391**

3.7.3 Interest rate risk

The table below summarises the Bank's exposure to interest rate risk. The assets and liabilities are recorded at carrying value, while the residual maturity is presented by contractual maturity for fixed-rate positions and by next contractual re-pricing date for floating rate positions.
Since for the fixed interest rate positions it is assumed that after contractual expiring will be reinvested or refinanced according to then prevailing market conditions, they were also included in the table herein below presenting the sensitivity to interest rate risk.

Interest rate risk

(in thousands of euros)

As at 31 December 2016	Carrying amount	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years	Non- interest bearing
ASSETS							
Cash and balances with central banks and other demand deposits at banks	192,843	135,127	-	-	-	17,449	40,267
Financial assets held for trading:	64	-	64	-	-	-	-
- derivative financial instruments	64	-	64	-	-	-	-
Financial assets measured at fair value through profit or loss	136	-	-	-	-	-	136
Derivatives – Hedge accounting	913	614	46	253	-	-	-
Available for sale financial assets	354,615	11,419	11,116	127,685	130,863	59,028	14,504
Loans and receivables:	1,726,905	205,558	211,145	1,089,955	68,171	125,534	26,542
- loans to banks	89,516	21,526	7,984	60,006	-	-	-
- loans to non-bank customers	1,626,373	184,032	203,161	1,029,949	68,171	125,534	15,526
- advances	11,016	-	-	-	-	-	11,016
Total assets	**2,275,476**	**352,718**	**222,371**	**1,217,893**	**199,034**	**202,011**	**81,449**
LIABILITIES							
Financial liabilities measured at amortised cost:	2,017,524	1,503,609	180,134	268,995	36,094	1,578	27,114
- deposits from banks and central banks	62,700	1,037	9,998	51,665	-	-	-
- deposits from non-bank customers	1,839,935	1,476,884	108,060	217,319	36,094	1,578	-
- loans from banks and central banks	87,747	25,685	62,062	-	-	-	-
- loans from non-bank costumers	28	3	14	11	-	-	-
- other financial liabilities	27,114	-	-	-	-	-	27,114
Derivatives – Hedge accounting	1,402	1,283	119	-	-	-	-
Total liabilities	**2,018,926**	**1,504,892**	**180,253**	**268,995**	**36,094**	**1,578**	**27,114**
Total interest repricing gap		**(1,152,788)**	**42,072**	**948,645**	**162,940**	**200,433**	

As at 31 December 2015	Carrying amount	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years	Non- interest bearing
Total assets	2,219,403	329,256	329,589	1,114,186	185,533	76,263	184,576
Total liabilities	1,971,710	1,332,597	273,199	310,497	29,492	3,329	22,596
Total interest repricing gap		**(1,003,341)**	**56,390**	**803,689**	**156,041**	**72,934**	

The Bank measures the following sources of interest rate risk:

- Repricing risk, stemming from a different interest rate adjustment of assets and liabilities to market interest rate changes. For fixed rate contracts the interest rate can be adjusted to market rate only at maturity, while floating rate contracts are adjusted according to contract revision of the interest rate and adjustment to market reference rate;
- Basis risk arises from imperfect correlation between different types of interest rates, which are relevant market rate reference for floating rate contracts;

Interest rate risk is measured from two perspectives: it is analysed through the impact of market rate change on net present value of future cash flows and, on the other hand, it is viewed through the impact of market rate changes on net interest income and therefore on the Bank's annual financial results.

Accordingly, the following data are reported to the ALCO:

- Sensitivity of net interest income to a yield curve parallel shift of +/-50 bps over a 1-year time horizon;
- Sensitivity of economic value or net present value of future cash flows to a yield curve parallel shift of +/- 100 bps and +/- 200 bps;

The measurement of Interest rate risk is further improved by using the following models:

- Sight model: Assets without contractual maturities are classified into specific time buckets based on their estimated sensitivity on changes in interest rates.
- Prepayment model based on the probability that some of the loans outstanding will be paid off earlier than originally scheduled. Consequently, the planned cash flows of the outstanding loans are modified for the level of prepayment rate.
- Excepted loss model: cash flows of outstanding loans are modified for the probability of default rate originating from credit risk.
- Fund Transfer Pricing model: the entire spread on loans above the reference rate is divided into cost of funding and commercial spread. For interest-sensitive cash flows only the spread representing cost of funding is taken.

Sensitivity of net interest income of the Bank as of 31. 12. 2016

(in million of euros)

		+50 b.p.			+100 b.p.			-50 b.p.			-100 b.p.		
		Sight	Term	Total	Sight	Term	Total	Sight	Term	Total	Sight	Term	Total
Total		**(0.82)**	**4.37**	**3.55**	**(4.02)**	**8.77**	**4.75**	**(0.72)**	**(4.03)**	**(4.75)**	**(1.46)**	**(7.47)**	**(8.93)**
Asset		**0.93**	**5.31**	**6.24**	**1.92**	**10.64**	**12.56**	**(0.90)**	**(4.96)**	**(5.86)**	**(1.80)**	**(9.34)**	**(11.14)**
Sight Loans		0.93		0.93	1.92		1.92	(0.90)		(0.90)	(1.80)		(1.80)
Securities	FX		0.16	0.16		0.33	0.33		(0.16)	(0.16)		(0.33)	(0.33)
	FL		0.22	0.22		0.45	0.45		(0.20)	(0.20)		(0.28)	(0.28)
Loans	FX		0.55	0.55		1.09	1.09		(0.55)	(0.55)		(1.09)	(1.09)
	FL		4.38	4.38		8.77	8.77		(4.05)	(4.05)		(7.64)	(7.64)
Other Financial Assets	FX		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
	FL		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
Liabilities		**(1.75)**	**(1.90)**	**(3.65)**	**(5.94)**	**(3.79)**	**(9.73)**	**0.18**	**1.90**	**2.08**	**0.34**	**3.81**	**4.15**
Sight Deposits		(1.75)		(1.75)	(5.94)		(5.94)	0.18		0.18	0.34		0.34
Securities Issued	FX		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
	FL		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
Debts	FX		(1.50)	(1.50)		(3.00)	(3.00)		1.50	1.50		3.01	3.01
	FL		(0.40)	(0.40)		(0.79)	(0.79)		0.40	0.40		0.80	0.80
Other Financial Liabilities	FX		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
	FL		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
Derivatives			**0.96**	**0.96**		**1.92**	**1.92**		**(0.97)**	**(0.97)**		**(1.94)**	**(1.94)**

Sensitivity of net interest income of the Bank as of 31. 12. 2015

(in million of euros)

		+50 b.p.			+100 b.p.			-50 b.p.			-100 b.p.		
		Sight	Term	Total	Sight	Term	Total	Sight	Term	Total	Sight	Term	Total
Total		**(2.19)**	**2.09**	**(0.10)**	**(5.49)**	**5.30**	**(0.19)**	**0.18**	**(0.29)**	**(0.11)**	**0.31**	**(0.50)**	**(0.19)**
Asset		**0.80**	**3.70**	**4.50**	**2.06**	**9.36**	**11.42**	**(0.02)**	**(0.41)**	**(0.43)**	**(0.04)**	**(0.71)**	**(0.75)**
Sight Loans		0.80		0.80	2.06		2.06	(0.02)		(0.02)	(0.04)		(0.04)
Securities	FX		0.15	0.15		0.39	0.39		0.00	0.00		0.00	0.00
	FL		0.08	0.08		0.20	0.20		0.00	0.00		0.00	0.00
Loans	FX		0.64	0.64		1.50	1.50		(0.26)	(0.26)		(0.44)	(0.44)
	FL		2.83	2.83		7.27	7.27		(0.15)	(0.15)		(0.27)	(0.27)
Other Financial Assets	FX		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
	FL		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
Liabilities		**(2.99)**	**(1.69)**	**(4.68)**	**(7.55)**	**(4.22)**	**(11.77)**	**0.20**	**0.20**	**0.20**	**0.35**	**0.36**	**0.71**
Sight Deposits		(2.99)		(2.99)	(7.55)		(7.55)	0.20		0.20	0.35		0.35
Securities Issued	FX		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
	FL		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
Debts	FX		(1.22)	(1.22)		(3.10)	(3.10)		0.08	0.08		0.15	0.15
	FL		(0.47)	(0.47)		(1.12)	(1.12)		0.12	0.12		0.21	0.21
Other Financial Liabilities	FX		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
	FL		0.00	0.00		0.00	0.00		0.00	0.00		0.00	0.00
Derivatives			**0.08**	**0.08**		**0.16**	**0.16**		**(0.08)**	**(0.08)**		**(0.15)**	**(0.15)**

The margin sensitivity indicators for 2015 and 2016 are not fully comparable owing to changes in the methodology. Due to lasting negative levels for the market interest rates, the Bank introduced specific rules that allow adequate cash flow representation based on actual contractual interest rates and relevant yield curve shifts. The Bank newly applied 0% floors on contractual interest rates for customer's sight deposits when according to shift scenario the rates drop below zero rate in order to replicate actual circumstances on the market. In addition the sight deposit model has been updated, in order to rebuild the sensitivity maturities of sight deposit balances in consideration of significant changes to customers deposit structure and relative increase of the sight deposit balances by 532 mln EUR. The main changes in the demand deposit models are related to the re-estimation of stability features of demand deposits based on latest historical data and the extension of balance distribution from 5 to 10 years (3% of demand deposits are considered stable over a period longer than 5 years). In order to control quantitatively the Bank's interest margin risk, a limit of EUR -7.5 mln has been set up for a +/- 50bp interest rates change. The impact on Bank's interest margin due to market interest rate 50 bp quick jump according to data end of 2016 would be positive EUR 3.6 mln, while in case of an instantaneous 50 bp drop the impact would be negative EUR 4.8 mln. The higher sensitivity to rate decrease scenario is credited to limited possibility for the interest rate on liabilities to fall.

The impact of 100 bps interest rate parallel shift on net present value of the Bank' interest-bearing assets and liabilities, as at 31 December 2016

(in million of euros)

Currency	Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
EUR	**6.19**	(1.02)	2.57	2.91	0.97	0.54	0.22
USD	**0.24**	(0.04)	0.10	0.13	0.05	-	-
CHF	**0.18**	0.05	0.06	0.07	0.01	(0.01)	-
Other	**0.06**	0.01	0.02	0.02	0.01	-	-
Total Shift	**6.67**	**(1.00)**	**2.75**	**3.13**	**1.04**	**0.53**	**0.22**
Limit	**9.0**						
Utilization %	**74.06%**						

In the table is presented the interest rate risk exposure of the Bank in terms of shift sensitivity, which measures the change of net present value of future cash-flows, as a result of parallel shift of market yield curve by 100 b.p. Each time-bucket shows the impact of interest rate change on net present value of cash-flows, distributed by time tenors according to residual time to the next repricing. The most significant exposure is in EUR currency, while the risk for other currencies is less material. The total exposure limit for +100 bps shift sensitivity amounts to 9.0 million EUR, while the actual exposure at reference date is 6.7 million EUR. The previously mentioned update of the sight deposit model had a significant impact also on EV sensitivity measure. Due to larger proportion of the stable component of sight deposits, the sensitivity of the Bank in terms of Economic value turned negatively sensitive to interest rate drop.

In addition to the total exposure limit, limits for specific time buckets are set:

(in million of euros)

Time bucket	Limit	Exposure
0–18 months	+/- 6.0	(1.01)
from 19 months–5 years	+/- 8.0	5.88
>5 years	+/- 8.0	(1.79)

The impact of 100 bps interest parallel rate shift on net present value of the Bank's interest-bearing assets and liabilities, as at 31 December 2015

(in million of euros)

Currency	Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
EUR	**(6.44)**	(3.39)	0.84	2.02	(2.84)	(2.17)	(0.90)
USD	**(0.19)**	(0.17)	(0.13)	0.11	-	-	-
CHF	**(0.03)**	(0.05)	-	0.04	(0.01)	(0.01)	-
Other	**0.03**	-	0.01	0.02	-	-	-
Total Shift	**(6.63)**	**(3.61)**	**0.72**	**2.19**	**(2.85)**	**(2.18)**	**(0.90)**
Limit	**9.0**						
Utilization %	**73.55%**						

The impact of +200 bps interest parallel rate shift on net present value of the Bank's interest-bearing assets and liabilities, as at 31 December 2016

(in million of euros)

Currency	Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
EUR	**11.75**	(2.80)	5.42	5.81	1.85	1.02	0.45
USD	**0.45**	(0.09)	0.20	0.25	0.09	-	-
CHF	**0.34**	0.06	0.11	0.15	0.04	(0.01)	(0.01)
Other	**0.11**	0.02	0.03	0.04	0.02	-	-
Total Shift	**12.65**	**(2.81)**	**5.76**	**6.25**	**2.00**	**1.01**	**0.44**
Reg,Capital (Sept 15)	**257.88**						
15% of Reg. Capital	**4.91%**						

The impact of +200 bps interest parallel rate shift on net present value of the Bank's interest-bearing assets and liabilities, as at 31 December 2015

(in million of euros)

Currency	Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
EUR	**(11.12)**	(5.52)	1.66	3.95	(5.47)	(4.10)	(1.64)
USD	**(0.37)**	(0.34)	(0.24)	0.21	-	-	-
CHF	**0.00**	(0.07)	0.03	0.09	(0.02)	(0.02)	(0.01)
Other	**0.08**	0.01	0.03	0.04	-	-	-
Total Shift	**(11.41)**	**(5.92)**	**1.48**	**4.29**	**(5.49)**	**(4.12)**	**(1.65)**
Reg,Capital (Sept 15)	**259.9**						
20% of Reg. Capital	**4.4%**						

The 200 bp shift is a standard measure defined by Banking supervisor that treats an impact thereof on Economic value that exceeds 15% Tier I capital as outlying excessive risk exposure. As of 31.12.2016 the sensitivity reached 4.91% of Tier I capital.

The table below summarises the effective annual interest rate for monetary financial instruments not carried at fair value through profit or loss by major currency:

The effective annual interest rate of individual financial instruments

	2016			2015		
	EUR	USD	Other	EUR	USD	Other
Assets						
Cash and balances at central banks and other demand deposits at banks	1.00	1.00	1.00	1.00	0.40	1.00
Loans and advances to banks	0.01	3.08	0.89	0.11	1.45	1.06
Loans and advances to non-bank customers	2.29	3.72	1.02	2.74	3.20	0.94
Available for sale financial assets	2.18	4.28	-	2.49	4.19	-
Liabilities						
Deposits from banks and central banks	0.03	-	0.60	0.12	-	0.60
Deposits from non-bank customers	0.13	0.10	0.01	0.32	0.11	0.01
Other borrowed funds	1.71	2.61	-	1.48	2.09	-

3.8 OPERATIONAL RISK

Operational risk is defined as the risk of direct or indirect loss resulting from inadequate or failed internal processes, systems, human behaviour or mistakes or from external events. The definition also includes legal risk, representing the risk of ineffective legal execution or defective legal documentation, as well as compliance risk, which is the risk of failure to comply with laws, rules, regulations, agreements and practices. However, the definition excludes strategic and reputational risk.

The objectives of operational risk management are to:
- Protect assets, preserve and safeguard material and intellectual Bank's assets.
- Control and proactively monitor processes to ensure that significant risks are swiftly identified.
- Comply with requirements and processes established with internal rules and external regulations.

The process of operational risk management comprises the identification, measurement or evaluation, control and monitoring of operational risk. The process of operational risk measurement and management is assisted by the risk mitigation tool developed by the parent company designed to support the carrying out of the following activities:
- Loss data collection,
- Business environment evaluation,
- Scenario analysis,
- Mitigation actions management, and
- Monitoring and reporting.

The systematic loss data collection makes it possible to perform immediate analysis of loss event causes and to adopt corrective actions. This procedure supports the compliance with general operational risk management standards.

First level operational risk management is carried out by the person directly responsible for operations in each organisational unit. The Risk Management Department, which is responsible for the operational loss data collection and the self-assessments activity with the involvement of the Level 1 organisational units, is in charge of second level operational risk management processes. The self-assessment activity is necessary to explore the level of the Bank's exposure to operational risk and to evaluate the risk appetite measure.
The Risk Management Department assisted by the Operational Risk Group (composed of the persons responsible from the most important first-level organisational units), reports on a quarterly basis to the Management Board and proposes remedial actions.

3.9 FAIR VALUE OF ASSETS AND LIABILITIES

Fair value of assets and liabilities

(in thousands of euros)

	2016			2015		
	Carrying value	Fair value	Unrecognised gain/loss	Carrying value	Fair value	Unrecognised gain/loss
ASSETS						
Cash, cash balances at central banks and other demand deposits at banks	192,843	192,843	-	234,240	234,240	-
Financial assets held for trading:	64	64	-	91	91	-
- derivative financial instruments	64	64	-	91	91	-
Financial assets designated at fair value through profit or loss	136	136	-	222	222	-
Available for sale financial assets	354,615	354,615	-	330,088	330,088	-
Derivatives-hedge accounting	913	913	-	21	21	-
Loans and receivables:	1,726,905	1,729,175	2,270	1,654,741	1,653,599	(1,142)
- loans to banks	89,516	89,516	-	160,140	160,140	-
- loans to non-bank customers	1,626,373	1,628,643	2,270	1,482,682	1,481,540	(1,142)
- advances	11,016	11,016	-	11,919	11,919	-
Other assets	13,389	13,389	-	11,712	11,712	-
Total assets	**2,288,865**	**2,291,135**	**2,270**	**2,231,115**	**2,229,973**	**2,231,115**
LIABILITIES						
Financial liabilities held for trading:	-	-	-	1	1	-
- derivative financial instruments	-	-	-	1	1	-
Financial liabilities measured at amortised cost:	2,017,524	2,017,243	(281)	1,971,643	1,970,961	(682)
- deposits from banks and central banks	62,700	62,807	107	22,821	22,952	131
- deposits from non-bank customers	1,839,935	1,839,915	(20)	1,776,685	1,776,271	(414)
- loans from banks and central banks	87,747	87,380	(367)	149,481	149,083	(398)
- loans from non-bank customers	28	27	(1)	60	59	(1)
- other financial liabilities	27,114	27,114	-	22,596	22,596	-
Derivatives-hedge accounting	1,402	1,402	-	66	66	-
Other liabilities	4,660	4,660	-	3,734	3,734	-
Total liabilities	**2,023,586**	**2,023,305**	**(281)**	**1,975,444**	**1,974,762**	**(682)**

Fair value of financial instruments

Derivatives

Accounting for derivatives at fair value is performed on the basis of observable market inputs. Derivative financial instruments subject to valuation are: interest rate swaps, interest rate caps, foreign exchange swaps, forward foreign exchange contracts. The fair value of derivatives is determined with the support of Murex, a system developed by the parent company. The system takes input data from the money market official quotations and from Reuters system. The fair value of interest rate swaps is the net present value of future cash flows, based upon spot and forward money market interest rates. The fair value of more complex derivatives such as caps is calculated by the parent company and is measured using the Black's Model with SABR volatility.

Hedge accounting

The Bank's interest rate policy course is to hedge in accordance with hedge accounting rules the interest rate risk assumed on each single large financial investments and loan clusters with similar characteristics and fixed rate remuneration (housing loans). For single large financial investments a micro fair value hedge is applied, while for housing loans the Bank engage in a macro fair value hedge. The loans eligible for hedging are chosen at the time of disbursement as having medium/long term contractual maturity and fixed rate remuneration. The identified loans are hedged with interest rate swap derivative contracts, conceding the transformation of fixed contractual rate to rate floating according to market benchmark, i.e. Euribor. The interest rate risk is hedged using the fair value method and the effectiveness of the hedging relationship is regularly measured by calculating the prospective and retrospective efficiency tests. For the prospective test the Bank measures the relation between interest rate sensitivity of the derivative instrument and sensitivity of the hedged item. In the retrospective test the 'Dollar offset method" is used, where the fair value changes of derivative instrument is compared to the fair value change of the hedged item. The ratio between the change of value for two items has to be within 80% and 125% range.

For the macro fair value hedges two efficiency tests are carried out in addition. The sensitivity test (first level test) is aimed at the verification that the sensitivity of the portfolio, subject to hedging and distributed by time buckets, is greater (in absolute terms) than the sensitivity of the hedging derivative instrument. The fair value capacity test (second level) is on the other hand necessary to assess the hedge effectiveness from a view of a dynamic management of the portfolio. The test verifies that the portfolio subject to hedging contains assets with sensitivity profile and expected fair value variations on hedged risk that is matching the hedging derivative.

According to the efficiency tests, as of 31 December 2016, all hedges were efficient.

As of 31 December 2016 the Bank had 18 interest rate swap (IRS) contracts, 16 of which underwritten in 2016, out of which 11 bonds, 4 mortgage portfolios and 3 large single loans

Hedged item	Nominal amount (in mln EUR)			Number of IRS contracts		
	2016	2015	Total	2016	2015	Total
Fixed income bond-micro hedge	78.5	20	98.5	9	2	11
Housing loans packages-macro hedge	37	-	37	4	-	4
Individual loans-micro hedge	89	-	89	3	-	3
Total	**204.5**	**20**	**224.5**	**16**	**2**	**18**

The fair value of all Bank`s IRS contracts` as of 31 December 2016 amounted to -0.489 mln EUR.

Financial instruments available for sale

Currently, the Bank's portfolio containing available-for-sale financial assets (AFS) is composed of bonds and shares. Both instruments are measured at fair value.

The fair value of bonds is derived from their quoted market prices.

The fair value of shares listed on the active stock market is their market value, whereas for the non-listed shares or illiquid shares, the fair value is determined using the internal valuation model. The internal valuation is carried out by applying the price multiples method. The difference between the model and market valuation when shares are quoted on illiquid market (currently only 1 such position), as at 31 December 2016 amounted to 136 thousand euros.

The basis for the calculation under the above method are the available market valuations of comparable enterprises, in connection with financial ratios and multiples of their traded shares in the valuation of non-traded or illiquid shares. A condition for the application of the method is the availability of at least two comparable enterprises with listed shares. The latter shall be comparable by industry, market capitalisation, size and geographical location.

Information on financial ratios (price multiples) for comparable enterprises shall be obtained from independent sources, such as the Ljubljana Stock Exchange, Reuters, etc.

The share value is based on the following price multiples of comparable enterprises:
- EV/S (enterprise value / sales);
- EV/EBITDA (enterprise value / EBIT + depreciation);
- P/E (price-to-earnings);
- P/BV (price / book value);

The basis for the estimation are the financial statements of the comparable enterprises:
- balance sheet (for the preceding 3 financial years);
- income statement (for the preceding 3 financial years).

The final value is computed as the average of the multiples, whereby multiples considered as inadequate, are omitted.

Breakdown of financial instruments measured at fair value into fair value hierarchy levels

(in thousands of euros)

	2016				2015			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Asset								
Derivatives	-	64	-	**64**	-	91	-	**91**
AFS:	327,575	25,113	1,927	**354,615**	691	320,452	8,945	**330,088**
- debt	316,177	23,934	-	**340,111**	-	307,907	-	**307,907**
- equities	11,398	1,179	1,927	**14,504**	691	12,545	8,945	**22,181**
FVTPL – equities	136	-	-	**136**	222	-	-	**222**
Loans and receivables	-	183,532	1,543,373	**1,726,905**	-	276,755	1,377,986	**1,654,741**
Liabilities								
Derivatives	-	-	-	**-**	-	1	-	**1**
Financial liabilities, measured at amortised cost	-	1,586,634	430,890	**2,017,524**	-	1,421,904	549,739	**1,971,643**

Movement of financial instrument included in level 3

(in thousands of euros)

	At January 2016	Purchase/ Sales	Unrealized gains/losses recorded in P&L	Unrealized gains/ losses recorded in revaluation reserve	Realized gains/ losses recorded in P&L	Transfers out of level 3	Transfers into level 3	At 31 December 2016
Asset								
AFS equities	8,945	(8,728)	-	-	-	-	1,710	1,927

Movement of financial instrument included in level 3

(in thousands of euros)

	At January 2015	Purchase/ Sales	Unrealized gains/losses recorded in P&L	Unrealized gains/ losses recorded in revaluation reserve	Realized gains/ losses recorded in P&L	Transfers out of level 3	Transfers into level 3	At 31 December 2015
Asset								
AFS equities	5,522	-	-	3,423	-	-	-	8,945

As of 31 December 2016, the Bank held in the investment portfolio 26 bonds measured at fair value (Available for Sale), out of which 4 measured with marked to model approach (level 2), while 22 were measured on market prices (level 1). As for equity portfolio all positions were valued with a marked to model approach, except for Cinkarna Celje, which is valued with a Mark to Market approach.

4. NET INTEREST INCOME

(in thousands of euros)

	2016	2015
Interest income		
Central bank deposits	2	8
Loans and advances (including finance leases):	43,240	49,948
- to banks	227	400
- to other customers	43,013	49,548
Investment securities (AFS)	4,903	5,993
Derivatives – hedge accounting	1,375	448
Other	34	2
Total	**49,554**	**56,399**
Interest expense		
Financial liabilities measured at amortised cost:		
- Bank deposits and borrowings	15	43
- Other customers	3,475	8,775
- Other borrowed funds	1,871	2,545
Derivatives - hedge accounting	1,702	585
Derivatives - HFT	-	111
Other	963	234
Total	**8,026**	**12,293**
Total	**41,528**	**44,106**

Within other interest income the Bank realised from financial liabilities EUR 8 thousand (2015: nil) as the consequences of negative interest rate.
Within other interest expense the Bank realised from financial assets EUR 959 thousand (2015: EUR 230 thousand) as the consequences of negative interest rate.

5. DIVIDEND INCOME

(in thousands of euros)

	2016	2015
Investment securities	638	541
Dividends from FVPL shares	17	4
Total	**655**	**545**

6. NET FEE AND COMMISSION INCOME

(in thousands of euros)

	2016	2015
Fee and commission income		
From current bank account management	3,903	3,898
From payment services	10,460	10,365
From credit card business	8,572	8,326
From interbanking operations	5,836	8,330
From loans granted	4,145	4,232
From guarantees given	1,404	1,527
From safe renting	86	74
From pension fund management	493	547
Depositary services	994	1,097
From payment systems management	1,526	1,697
From brokering of loans and insurance contract on behalf of others	239	185
Total	**37,658**	**40,278**
Fee and commission expense		
For security trading	61	54
For loan brokerage on behalf of others	113	145
For custody services	384	415
For credit card processing	8,263	10,413
For payment transactions	2,888	2,615
Commitment fee for unused credit lines	151	173
Total	**11,860**	**13,815**
Total	**25,798**	**26,463**

7. REALISED GAINS AND LOSSES OF FINANCIAL ASSETS AND LIABILITIES NOT MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS

(in thousands of euros)

	2016	2015
Loss/income due to sale of investment securities*	19,680	4,407
Write offs of loans and other assets	(106)	(1,809)
Total	**19,574**	**2,598**

**From released revaluation reserve EUR 6,446 thousand (2015: EUR 4,235 thousand).*

In 2016 the Bank sold two equity investments from which realised a gain of EUR 16,119 thousand.

8. GAINS AND LOSSES OF FINANCIAL ASSETS AND LIABILITIES HELD FOR TRADING

(in thousands of euros)

	2016	2015
Trading of derivatives	(24)	51
Currency trading	836	990
Total	**812**	**1,041**

9. FAIR VALUE ADJUSTMENTS IN HEDGE ACCOUNTING

(in thousands of euros)

	2016	2015
Net effect on derivatives used as hedging instruments	(36)	92
Net effect on hedged items	172	(184)
Total	**136**	**(92)**

Derivatives used as hedge instruments and the nature of hedged items are additionally explained in note 20 and in note 3.9. Fair value of assets and liabilities (in paragraph hedge accounting).

10. GAINS AND LOSSES ON DERECOGNITION OF ASSETS

(in thousands of euros)

	2016	2015
Profit on sale of property and equipment	1,043	47
Total	**1,043**	**47**

11. OTHER OPERATING NET INCOME

(in thousands of euros)

	2016	2015
Rents	3,107	3,241
Proceeds from the sale of repossessed leased assets	(186)	23
Taxes	(383)	(421)
Membership fees	(82)	(82)
Contribution to European Banking Resolution Fund	(577)	(733)
Contribution to European Deposit Guarantee Scheme	(1,589)	-
Expenses related to operating and financial leasing	(173)	(227)
Expenses from investment property under the operating lease	(307)	(260)
Other	13	20
Total	**(177)**	**1,561**

From rent contracts arises that the future rent revenues will amount to EUR 19,100 thousand (2015: EUR 17,700 thousand), as follows:

(in thousands of euros)

2016			2015		
Up to 1 year	**1 to 5 years**	**Over 5 years**	**Up to 1 year**	**1 to 5 years**	**Over 5 years**
1,910	7,640	9,550	1,770	7,080	8,850

12. ADMINISTRATIVE EXPENSES

(in thousands of euros)

	2016	2015
Staff cost	**27,957**	**28,469**
Salaries	18,892	18,956
Social security	3,022	3,066
Contributions to the pension scheme	1,692	1,679
Other	4,351	4,768
Other administrative expenses	**12,293**	**12,081**
Material costs	2,027	2,087
IT costs	2,889	2,065
Rents	1,507	1,455
Professional services	1,471	1,842
Advertising and marketing	509	618
Consulting, auditing, legal and notarial fees*	351	443
Maintenance, governance and security of tangible fixed assets	1,092	1,176
Postal services and rent of communication lines	1,619	1,644
Insurance	371	378
Travel costs	47	55
Education, scholarships and tuition fees	146	148
Bank's supervision	264	170
Total administrative expenses	**40,250**	**40,550**

**Of which audit of the Bank's financial statements EUR 109 thousand (2015: EUR 100 thousand)*

13. DEPRECIATION AND AMORTISATION

(in thousands of euros)

	2016	2015
Amortisation	1,309	1,695
Depreciation	3,383	3,727
Total	**4,692**	**5,422**

14. PROVISIONS AND POST-EMPLOYMENT BENEFIT OBLIGATIONS

(in thousands of euros)

	2016	2015
Provisions for off-balance sheet exposures	1,858	190
Provisions for legal proceedings and future contract obligations	(300)	(18)
Retirement and long service bonuses	(435)	(415)
Total	**1,123**	**(243)**

Income from provisions for off balance sheet exposures arise from excess of recovered provisions as a result of changes in the calculation of provisions. According to Group Accounting Manual performing off-balance sheet exposures are diluted by credit conversion factor in the procedure of provision calculation.

The movement of provisions and post-employment benefit obligations is shown in note 34 and 35.

15. IMPAIRMENT

(in thousands of euros)

	2016	2015
Impairments on assets measurement at amortised cost:	32	
- loans to other customers	20,175	14,395
- impairments of other assets	178	497
Impairments on AFS securities (shares)	299	-
Impairments on land seized for repayment of loans	1,033	935
Impairments on investment property	522	-
Total	**22,239**	**15,827**

Increase in impairments on loans to other customers is due to drop of collateral value (see note 3.4).

16. TAX EXPENSE (INCOME) RELATED TO PROFIT OR LOSS FROM CONTINUING OPERATIONS

(in thousands of euros)

	2014	2015
Current tax	1,009	-
Deferred tax (note 37)	1,710	2,335
Total	**2,719**	**2,335**
Profit before tax	**22,959**	**14,198**

Further information about deferred income tax is presented in note 36. The tax on the Bank's profit before tax differs from the theoretical amount that would arise using the basic tax rate as follows:

(in thousands of euros)

	2016	2015
Prima facie tax calculated at a tax rate of 17%	3,903	2,414
Income from already taxed released provisions	-	(2)
Income form already taxed dividends	(111)	(93)
Income from sale of equity investments	(944)	-
Expenses not deductible for tax purposes:		
- staff costs not assessable for tax	148	157
- other non-tax deductible expenses	81	72
Actuarial losses recognised trough other comprehensive income	7	(59)
Tax reliefs, that can be carried forward	(284)	(134)
Effect of tax rate increase from 17 % to 19 %	(81)	-
Total income tax	**2,719**	**2,355**

For 2016 the income tax rate was 17% (2015: 17%) as prescribed by law.
In 2015, due to realised tax loss, current tax is nil. Tax loss is the result of cancellation of impairments of AFS financial assets due to the sale of financial assets and expropriation.

In accordance with local regulations, the Financial Administration may at any time inspect the Bank's books and records within the 5 years subsequent to the reported tax year and may impose additional tax assessments and penalties. The Bank's management is not aware of any circumstances which may give rise to a potential material liability in this respect.

17. EARNINGS PER SHARE

(in thousands of euros)

	2016	2015
Net profit for the year	20,240	11,843
Weighted average number of ordinary shares in issue	530,398	530,398
Basic and diluted profit per share (in EUR per share)	**38.16**	**22.33**

Basic earnings per share is calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year, excluding the average number of ordinary shares purchased by the Bank and held as treasury shares (961 lots). There are no dilutive potential ordinary shares, there are no share options schemes.

18. INCOMES AND EXPENSES ACHIEVED ON FOREIGN MARKETS

Income and expenses realised on a foreign markets mostly related to clients from EU state members.

(in thousands of euros)

	2016	2015
Interest income	4,858	4,540
Interest expenses	(4,033)	(4,670)
Net Interest income	**825**	**(130)**
Fee and commission income	536	646
Fee and commission expenses	(1,385)	(994)
Net fee and commission income	**(849)**	**(348)**
Gains or losses on financial assets and liabilities held for trading	165	114
Fair value adjustments in hedge accounting	(88)	22
Realised gains or losses on financial assets and liabilities not measured at fair value through profit or loss	16,120	4
Gains or losses on financial assets and liabilities designated at fair value through profit or loss	(48)	71
Other operating net income	2	(50)
Other administrative expenses	(1,857)	(605)
Total profit or loss before tax from continuing operations	**14,270**	**(922)**

19. CASH, CASH BALANCES AT CENTRAL BANKS AND OTHER DEMAND DEPOSITS AT BANKS

(in thousands of euros)

	2016	2015
Cash in hand	16,114	15,620
Balances with central banks	136,466	75,346
Other sight deposits	40,279	143,274
Gross cash, cash balances at central banks and other demand deposits at banks	**192,859**	**234,240**
Impairment	(16)	-
Net cash, cash balances at central banks and other demand deposits at banks	**192,843**	**234,240**
From this: mandatory reserve liability to central banks	17,449	16,194

The Bank is required to maintain a mandatory reserve with the central bank (Bank of Slovenia), relative to the volume and structure of its customer deposits. The current requirement of the Bank of Slovenia regarding the calculation of the amount to be held as mandatory reserve is 1% of time deposits and issued debt securities with maturities up to two years.

The Bank maintains sufficient liquid assets to fully comply with the central bank requirements.

20. DERIVATIVE FINANCIAL INSTRUMENTS

The majority of derivative contracts is entered into for the purpose of interest-rate risk management. A derivative instrument is entered into as an economic hedge where its terms and conditions are a mirror image of the terms and conditions of the hedged financial instruments. In addition, the Bank also uses fair value hedge accounting techniques, where interest rate swaps hedges long-term financial assets (bonds and loans) with fixed interest rate. The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of these instruments and, therefore, do not indicate the Bank's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in the reference rate or index relative to their terms. The aggregate contractual or notional amount of derivative financial instruments, the extent to which instruments are favourable or unfavourable and, thus the aggregate fair values of derivative financial assets and liabilities can fluctuate significantly from time to time. The notional amount and fair values of derivative instruments held for trading and designated as hedges are set out in the following tables:

Derivative financial instruments

(in thousands of euros)

As at 31 December 2016	Notional amount	Fair value	
		Assets	Liabilities
Interest rate			
Interest rate cap (CALL)	6,028	64	-
Interest rate cap (PUT)	800	-	-
Total held for trading derivatives		**64**	**-**
Hedging derivatives			
Interest rate swaps (IRS) – micro hedge	185,384	565	1,363
Interest rate swaps (IRS) – macro hedge	35,912	348	39
Total derivative for hedge accounting		**913**	**1,402**

(in thousands of euros)

As at 31 December 2015	Notional amount	Fair value	
		Assets	Liabilities
HFT derivatives			
Foreign exchange rate			
Forwards-purchase	76	-	-
Forwards-sale	76	-	-
Interest rate			
Interest rate cap (CALL)	6,418	91	-
Interest rate cap (PUT)	950	-	1
Total held for trading derivatives		**91**	**1**
Hedging derivatives			
Interest rate swaps (IRS) – micro hedge	18,305	21	66
Total derivative for hedge accounting		**21**	**66**

In financial environment of low interest rates the Bank promoted its commercial activities by lunching long term loans fix interest rates. To overcome the interest rate risk interest rate swaps were made.

21. AVAILABLE-FOR-SALE FINANCIAL ASSETS

(in thousands of euros)

	2016	2015
Government securities:		
- listed	310,730	275,873
Other debt securities:		
- listed	29,381	32,035
Equity securities:		
- listed	1,525	1,444
- unlisted	2,353	10,122
Investment in National Bank Resolution Fund	10,626	10,614
Total securities available-for-sale	**354,615**	**330,088**

The Bank adopted its own valuation model in cases where investments are not listed or measures such investments at cost less impairments.

In order to comply with the requirements of the National Bank Resolution Fund, Slovenian government bonds in the amount of EUR 10.9 million are encumbered.

Movement

(in thousands of euros)

	2016 AFS	2015 AFS
At beginning of the year	**330,088**	**297,357**
Additions	128,421	176,385
Impairment	(299)	-
Interest accrual	9,327	10,037
Expired coupons	(9,288)	(11,452)
Disposals (sale and redemption)	(95,002)	(138,471)
Gains/losses from changes in fair value	(9,427)	(3,768)
Exchange differences	795	-
At end of year	**354,615**	**330,088**

22. LOANS TO BANKS

(in thousands of euros)

	2016	2015
Placements with other banks	89,532	160,140
Gross loans to banks	**89,532**	**160,140**
Impairment	(16)	-
Total loans to banks	**89,516**	**160,140**

As at 31 December 2016 no placements with other banks are shown under Pledged assets (2015: nil).

23. LOANS TO NON-BANK CUSTOMERS

(in thousands of euros)

	2016	2015
Loans to individuals:	**542,166**	**517,676**
- Overdrafts	25,838	29,677
- Credit cards	18,281	18,993
- Term loans	102,780	100,187
- Mortgages	387,128	358,716
- Financial leases	8,139	10,103
Loans to sole proprietors	**58,930**	**63,988**
Financial leases	10,655	13,555
Other loans	48,275	50,433
Loans to corporate entities	**1,129,648**	**1,041,900**
Financial leases	56,341	80,416
Other loans	1,073,307	961,484
Gross loans and advances	**1,730,744**	**1,623,564**
Less provision for impairment	(104,371)	(140,882)
Net loans and advances	**1,626,373**	**1,482,682**

Movement in provisions for impairment losses on loans to retail customers as follows

(in thousands of euros)

	Loans to individuals					
	Overdrafts	Credit cards	Term loans	Mortgages	Finance leases	Total loans to individuals
As at 31 December 2014	**1,171**	**844**	**1,619**	**2,830**	**-**	**6,464**
Provision for loan impairment	720	813	823	2,447	148	4,951
Amounts recovered during the year	(713)	(888)	(832)	(1,649)	(162)	(4,244)
Included in income statement	7	(75)	(9)	798	(14)	707
Increase of impairments due to Finor Leasing's merger	-	-	-	-	444	444
Write off	(224)	-	(53)	(55)	-	(332)
As at 31 December 2015	**954**	**769**	**1,557**	**3,573**	**430**	**7,283**
Provision for loan impairment	530	697	992	2,560	371	5,150
Amounts recovered during the year	(413)	(752)	(469)	(1,989)	(514)	(4,137)
Included in income statement	117	(55)	523	571	(143)	1,013
Write off	(55)	-	(58)	(1)	-	(114)
As at 31 December 2016	**1,016**	**714**	**2,022**	**4,143**	**287**	**8,182**

Movement in provisions for impairment losses on loans to corporate customers as follows

(in thousands of euros)

	Sole proprietors	Corporate entities
As at 31 December 2014	**7,698**	**129,376**
Provision for loan impairment	2,157	41,809
Amounts recovered during the year	(1,974)	(28,304)
Included in income statement	183	13,505
Increase of impairments due to Finor Leasing's merger	656	4,477
Write off	(1,469)	(20,805)
Impairment on capitalised suspended interest	-	(22)
As at 31 December 2015	**7,068**	**126,531**
Provision for loan impairment	2,957	49,365
Amounts recovered during the year	(2,903)	(30,257)
Included in income statement	54	19,108
Write off	(17)	(56,555)
As at 31 December 2016	**7,105**	**89,084**

In 2016 the Bank continued with the non-performing reduction plan, which is also in line with Bank of Slovenia Regulation criteria for write-offs in the assessment of credit risk losses.

Customer loan portfolio by economic sector

(in thousands of euros)

	2016	2015
Government	63,929	65,642
Trade	135,889	159,358
Services	462,360	354,520
Construction	52,199	66,042
Manufacturing	196,304	201,208
Agriculture	4,500	6,007
Individuals	542,166	517,676
Sole proprietors	58,931	63,988
Other	214,466	189,123
Gross loans and advances to customers	**1,730,744**	**1,623,564**
Less provision for impairment	(104,371)	(140,882)
Net loans and advances to customers	**1,626,373**	**1,482,682**

Slovenian customers and customers from selected European countries (Serbia, Croatia, Liberia, Albania, Italy) accounted for respectively 96% and 4% of geographic risk concentration within the customer loan portfolio.

Analysis of financial leases by residual maturity:

(in thousands of euros)

	2016	2015
Future minimum lease payments (financial leases):		
Not later than 1 year	25,031	32,444
Later than 1 year and not later than 5 years	35,010	51,093
Later than 5 years	15,094	20,537
	75,135	**104,074**
Present value of future minimum lease payments:		
Not later than 1 year	23,225	28,704
Later than 1 year and not later than 5 years	33,296	47,842
Later than 5 years	13,601	19,753
	70,122	**96,299**

Forborne exposures as at 31. 12. 2016

(in thousands of euros)

	General governments	Non-financial corporations	Households	Total
Performing exposures	-	47,816	1,097	48,913
Instruments with modifications in their terms and conditions	2,513	64,154	2,348	69,015
Refinancing	-	9,646	1,109	10,755
Total gross carrying amount	**2,513**	**121,616**	**4,554**	**128,683**
Performing	-	(4,871)	(50)	(4,921)
Instruments with modifications in their terms and conditions	(281)	(25,563)	(1,116)	(26,960)
Refinancing	-	(4,501)	(688)	(5,189)
Accumulated impairment, accumulated changes in fair value due to credit risk and provisions	**(281)**	**(34,935)**	**(1,854)**	**(37,070)**
Performing exposures	-	42,945	1,047	43,992
Instruments with modifications in their terms and conditions	2,232	38,591	1,232	42,055
Refinancing	-	5,145	421	5,566
Net carrying amount	**2,232**	**86,681**	**2,700**	**91,613**

In 2016 the Bank restructured loans in the amount of 27,914 thousands EUR (2015: EUR 47,305 thousands).

Forborne exposures as at 31. 12. 2015

(in thousands of euros)

	General governments	Non-financial corporations	Households	Total
Performing exposures	198	77,514	2,393	80,105
Instruments with modifications in their terms and conditions	3,827	43,220	1,424	48,471
Refinancing	-	5,810	2	5,812
Total gross carrying amount	**4,025**	**126,544**	**3,819**	**134,388**
Performing	(5)	(5,265)	(34)	(5,304)
Instruments with modifications in their terms and conditions	(841)	(12,817)	(655)	(14,313)
Refinancing	-	(2,437)	(1)	(2,438)
Accumulated impairment, accumulated changes in fair value due to credit risk and provisions	**(846)**	**(20,519)**	**(690)**	**(22,055)**
Performing exposures	193	72,249	2,359	74,801
Instruments with modifications in their terms and conditions	2,986	30,403	769	34,158
Refinancing	-	3,373	1	3,374
Net carrying amount	**3,179**	**106,025**	**3,129**	**112,333**

Forbearance measures are concessions made to a borrower facing or about to face financial difficulties by agreeing to change agreed contractual terms and conditions, so as to make them for the borrower more favourable than those that would be granted under normal conditions. Forbearance measures are conceded in order to maximize collection and minimize the risk of default. A forborne exposure can be performing or non-performing and related to retail or corporate customers.

According to the Bank regulations, individual loan contracts are flagged as exposures with forbearance measures for the purpose of evidencing the portfolio of forborne exposures, i.e., exposures which meet the above described definition. The forborne flag is therefore an additional element for classification of credit exposures for the purpose of credit portfolio monitoring and reporting. Taking into account the internal rules for the performing and non-performing exposures classification, rules governing the forborne exposures did not have a significant impact on the Bank's income statement.

Loans and advances are further analysed as a part of the statement of financial position in the accompanying notes: Analysis of past due financial instruments 3.4, Currency Risk Note 3.7.2., Interest Rate Risk Note 3.7,3., Liquidity Risk Note 3.5., Fair value Note 3.9., and Related Party Transactions Note 44.

24. ADVANCES

(in thousands of euros)

	2016	2015
Commissions receivables	391	337
Cheques	9	13
Receivables	646	898
Claims to Europay	5,334	6,832
Claims to citizens	807	898
Other	5,205	4,174
Gross advances	**12,392**	**13,152**
Impairments	(1,376)	(1,233)
Net advances	**11,016**	**11,919**

Movement in provisions for impairment on other assets:

(in thousands of euros)

As at 31 December 2014	**577**
Additional provision for impairment	900
Amounts recovered during the year	(403)
Included in income statement	497
Write off of impairment	(46)
Increase of impairments due to Finor Leasing's merger	205
As at 31 December 2015	**1,233**
Additional provision for impairment	251
Amounts recovered during the year	(73)
Included in income statement	178
Write off of impairment	(35)
As at 31 December 2016	**1,376**

25. PROPERTY, PLANT AND EQUIPMENT

(in thousands of euros)

	Land and buildings	Hardware equipment	Other equipment	Total
Net book amount as at 31 December 2014	**19,826**	**970**	**1,467**	**22,263**
Movement in year 2015				
Opening net book amount	**19,826**	**970**	**1,467**	**22,263**
Transfer to investment property	(332)	-	-	(332)
Transfer from investment property	281	-	-	281
Additions	476	254	1,998	2,728
Disposals	-	-	(16)	(16)
Depreciation charge	(1,907)	(443)	(1,051)	(3,401)
Closing net book amount	**18,344**	**781**	**2,398**	**21,523**
As at 31 December 2015				
Cost	51,359	6,010	13,392	70,761
Accumulated depreciation	(33,015)	(5,229)	(10,994)	(49,238)
Net book amount as at 31 December 2015	**18,344**	**781**	**2,398**	**21,523**

(in thousands of euros)

	Land and buildings	Hardware equipment	Other equipment	Total
Movement in year 2016				
Opening net book amount	18,344	781	2,398	21,523
Additions	6	344	206	556
Disposals	-	-	(315)	(315)
Depreciation charge	(1,920)	(378)	(766)	(3,064)
Closing net book amount	**16,430**	**747**	**1,523**	**18,700**
As at 31 December 2016				
Cost	51,365	5,734	12,426	69,525
Accumulated depreciation	(34,935)	(4,987)	(10,903)	(50,825)
Net book amount as at 31 December 2016	**16,430**	**747**	**1,523**	**18,700**

In 2016 there was no property, plant and equipment pledged (2015; nil).

In addition to its own premises, the Bank hired premises at 32 locations. Future minimum lease payments under lease contracts amount to EUR 5,550 thousand, of this:

(in thousands of euros)

2016			2015		
Up to 1 year	1 to 5 years	Over 5 years	Up to 1 year	1 to 5 years	Over 5 years
555	2,220	2,775	552	2,208	2,760

26. INVESTMENT PROPERTY

For Investment Property there are no special restrictions in terms of duration and use.

On 31 December 2016 no stipulated contracts for the acquisition or construction of Investment Property are in place in Banka Koper. Except of current maintenance, no substantial investments in the repair, maintenance or expansion of these investments are planned in 2017.

Movement in investment property

(in thousands of euros)

	2016	2015
At beginning of the year	**14,127**	**1,261**
Depreciation	(319)	(326)
Transfer from property in use	-	332
Transfer to property in use	-	(281)
Transfer to property in stock	(476)	-
Additions	1,251	13,141
Disposals	(598)	-
At end of year	**13,985**	**14,127**

In 2015 the increase of investment property relates to integration of Finor Leasing's business within the Bank.

In the item other operating gains and losses (see note 11) income from property investments carries rents of EUR 1,379 thousand (2015: EUR 760 thousand). In 2016, Bank`s maintenance costs for rented property investments amounted to EUR 316 thousand (2015: EUR 276 thousand), meanwhile the maintenance cost related to non-rented property investments amounted to EUR 7 thousand (2015: EUR 7 thousand).

The Bank owns 26 investment properties. They were obtained by closure of its activities in some branches or from seized collateral for the repayment of loans. For the largest of them, the Bank has obtained the valuation by an independent appraisal. The fair value of its investment property is estimated at EUR 14,231 thousand.

27. INTANGIBLE ASSETS

(in thousands of euros)

	Development	Licenses	Software and other	Total
Movement in year 2015				
Opening net book amount	2,705	927	733	4,365
Additions	1,399	235	167	1,801
Amortisation	(1,046)	(387)	(262)	(1,695)
Closing net book amount	**3,058**	**775**	**638**	**4,471**
As at 31 December 2015				
Cost	13,284	3,940	4,594	21,818
Accumulated amortisation	(10,226)	(3,165)	(3,956)	(17,347)
Net book amount as at 31 December 2015	**3,058**	**775**	**638**	**4,471**
Movement in year 2016				
Opening net book amount	3,058	775	638	4,471
Additions	557	186	162	905
Amortisation	(814)	(303)	(192)	(1,309)
Closing net book amount	**2,801**	**658**	**608**	**4,067**
As at 31 December 2016				
Cost	13,841	3,188	4,030	21,059
Accumulated amortisation	(11,040)	(2,530)	(3,422)	(16,992)
Net book amount as at 31 December 2016	**2,801**	**658**	**608**	**4,067**

The Bank has not pledged any intangible fixed assets.

The Bank does not have any intangible fixed assets in management.

In 2016, the Bank has not recognized any expenditure related to research and development in the income statement. All development expenditure in 2016 was capitalized as intangible fixed assets, out of which staff expenses amounted to EUR 340 thousand.

28. OTHER ASSETS

(in thousands of euros)

	2016	2015
Accruals	837	514
Inventory	18	19
Taxes and contributions	414	595
Fixed assets from seized collateral	12,095	10,362
Prepayments and bails	25	222
Total	**13,389**	**11,712**

Fixed assets from seized collateral related mainly to assets subject of leasing contracts.

29. DEPOSITS FROM BANKS AND CENTRAL BANKS

(in thousands of euros)

	2016	2015
Demand deposits	1,037	4,245
Term deposits	61,663	18,576
Total	**62,700**	**22,821**

30. DEPOSITS FROM NON-BANK CUSTOMERS

(in thousands of euros)

	2016	2015
Individuals		
- demand deposits	803,282	648,671
- term deposits	530,197	578,247
Sole proprietors		
- demand deposits	68,234	62,343
- term deposits	2,838	3,277
Corporate customers		
- demand deposits	374,005	358,297
- term deposits	61,379	125,850
Total	**1,839,935**	**1,776,685**

As at 31 December 2016, deposits in the amount of EUR 15,667 thousand have been pledged for covering potential credit risk on assets (2015: EUR 12,191 thousand).

31. LOANS FROM BANKS AND CENTRAL BANKS

The Bank repaid its obligations regularly. At the date of the financial statements, there are no obligations which are overdue.

(in thousands of euros)

	2016		2015	
	Short term	Long term	Short term	Long term
In local currency	-	66,853	-	123,767
In foreign currency	-	20,894	-	25,714
Total	-	**87,747**	**-**	**149,481**
	87,747		**149,481**	

32. LOANS FROM NON-BANK COSTUMER

(in thousands of euros)

	2016	2015
	Long term	Long term
Financial leases	28	60
Total	**28**	**60**

The residual maturity of the financial liability is shown in note 3.5. - Liquidity risk.

33. OTHER FINANCIAL LIABILITIES

(in thousands of euros)

	2016	2015
Unpaid commissions	133	161
Liabilities form credit card business	5,870	6,037
Not yet process payments	10,698	6,979
Unpaid dividend	118	110
Creditors	2,042	2,431
Salaries	2,020	2,047
Deferred income	5,834	4,349
Other	399	482
Total	**27,114**	**22,596**

34. PROVISIONS FOR LIABILITIES AND CHARGES

The Bank also makes credit risk provisions for off-balance sheet items. The above credit risk provisions recorded by Banka Koper refer to contractual commitments for issued guarantees and letters of credits and irrevocable contractual commitments for granted, but undrawn loans. The same principles as for provisions for on-balance sheet items are applied.

(in thousands of euros)

	2016	2015
Provisions for off-balance sheet liabilities	4,653	6,514
Legal proceedings due to employees	540	240
Total	**5,193**	**6,754**

As at 31 December 2016, the Bank was involved in several legal proceedings against it. Contingent liabilities in this respect are estimated in the amount of EUR 2,297 thousand. To this end, on the basis of its best estimation on the outcome of the legal proceedings, the Bank established provisions in the amount of EUR 540 thousand.

Movement in provisions:

(in thousands of euros)

	2016	2015
At beginning of year	**6,754**	**8,458**
Additional provision	5,706	10,401
Amounts recovered during the year	(7,264)	(10,573)
Included in income statement under provisions	(1,558)	(172)
Repayment of the premiums for National Saving Housing Scheme	(3)	(53)
Indemnities paid	-	(1)
Conversion of provisions to impairment on seized land for repayment of loans	-	(1,478)
At end of year	**5,193**	**6,754**

35. RETIREMENT BENEFIT OBLIGATIONS

(in thousands of euros)

	2016	2015
Retirement severance pay and long service bonuses	4,152	4,020
Provision for redundancies	706	580
	4,858	**4,600**

Movements:

(in thousands of euros)

	2016	2015
At beginning of year	**4,600**	**3,667**
Additional provisions	435	415
Charged to income statement	435	415
Actuarial losses	(78)	697
Utilised provisions	(99)	(232)
Provisions from Finor Leasing	-	53
At end of year	**4,858**	**4,600**

36. DEFERRED INCOME TAXES

Deferred tax liabilities:

(in thousands of euros)

	2016	2015
Non-current assets held for sale	2	2
Available-for-sale financial assets	1,574	2,302
Total	**1,576**	**2,304**

Deferred tax assets:

(in thousands of euros)

	2016	2015
Retirement and other employee benefits	422	372
Loan impairments on financial and operating leasing	164	473
Available-for-sale financial assets	303	202
Tax reliefs, that can be carried forward	-	134
Tax loss	-	1,380
Other - depreciation above tax prescribed rate	5	5
Total	**894**	**2,566**
Net deferred taxes	**682**	**262**

Movement in deferred taxes (offsetting of assets and liabilities):

(in thousands of euros)

	2016	2015
At beginning of year	(262)	(1,312)
Deferred taxes charged in income statement	1,710	2,355
AFS financial assets (fair value measurement)	(924)	(254)
Actuarial losses	7	(59)
Retirement and other employee benefits	-	(5)
Loan impairments on financial and operating leasing	-	(987)
Effect of tax rate increase from 17% to 19%	151	-
At end of year	**682**	**(262)**

Deferred taxes charged in income statement:

(in thousands of euros)

	2016	2015
Retirement and other employee benefits	13	(13)
Trading securities and derivative financial instruments	-	(4)
Provisions for National Saving Housing Scheme	-	(9)
Impairment on AFS financial assets	36	(3,329)
Other	(1)	-
Loan impairments on financial and operating leasing	(325)	(514)
Tax reliefs, that can be carried forward	(134)	134
Tax loss	(1,380)	1,380
Effect of tax rate increase from 17% to 19%		
- Employees benefits	38	-
- Impairment on AFS financial assets	25	-
- Loan impairments on financial and operating leasing	17	-
- Other	1	-
Total	**(1,710)**	**(2,355)**

37. OTHER LIABILITIES

(in thousands of euros)

	2016	2015
Accruals	1,647	1,086
Prepayments received	2,195	1,181
Taxes and contributions	818	1,467
Total	**4,660**	**3,734**

38. SHARE CAPITAL

(in thousands of euros)

	Number of shares	Ordinary shares	Share premium	Treasury shares
As at 31 December 2014	531,359	22,173	7,499	(49)
As at 31 December 2015	531,359	22,173	7,499	(49)
As at 31 December 2016	531,359	22,173	7,499	(49)

The share capital of the Bank is divided into 531,359 ordinary shares. Each share has an equal proportion in the share capital of the Bank and its participating value in the share capital as well. The proportion of each share in the share capital of the Bank is determined on the basis of the number of the issued shares.

39. ACCUMULATED OTHER COMPREHENSIVE INCOME

(in thousands of euros)

	2016	2015
Revaluation reserves:		
- Debt securities	6,037	8,268
- Equity securities	382	2,821
Actuarial losses	(560)	(638)
Total	**5,859**	**10,451**

(in thousands of euros)

Movement	Revaluation reserves
As at 31 December 2014	**12,331**
Valuation of available-for-sale securities	
Equity securities	**(402)**
- Valuation	2,512
- Disposals	(2,914)
Debt securities	**(839)**
- Valuation	(304)
- Disposals	(600)
- Valuation of hedge items transferred to profit or loss	65
Actuarial loss	**(638)**
As at 31 December 2015	**10,451**

(in thousands of euros)

	Revaluation reserves
As at 31 December 2015	**10,451**
Valuation of available-for-sale securities	
Equity securities	**(2,439)**
- Valuation	359
- Disposals	(2,875)
- Impairment	86
- Effect of tax rate increase	(9)
Debt securities	**(2,231)**
- Valuation	(52)
- Disposals	(2,474)
- Valuation of hedge items transferred to profit or loss	444
- Effect of tax rate increase	(149)
Other comprehensive income	**78**
Actuarial loss	71
Effect of tax rate increase	7
As at 31 December 2016	**5,859**

40. RESERVES FROM PROFIT AND RETAINED EARNINGS

(in thousands of euros)

	2016	2015
Legal reserves	15,260	14,248
Statutory reserves	214,053	213,357
Retained earnings	25,238	17,956
Treasury share`s reserves	49	49
Total	**254,600**	**245,610**

(in thousands of euros)

Movement	Legal reserves	Statutory reserves	Retained earnings	Treasury share`s reserves	Total reserves
As at 31 December 2014	**13,655**	**212,365**	**12,305**	**49**	**238,374**
Net profit for the financial year	-	-	11,843	-	11,843
Dividends	-	-	(5,304)	-	(5,304)
Transfer to statutory reserves	-	992	(992)	-	-
Transfer to legal reserves	593	-	(593)	-	-
Net result from merger by absorption of Finor Leasing	-	-	697	-	697
As at 31 December 2015	**14,248**	**213,357**	**17,956**	**49**	**245,610**
Net profit for the financial year	-	-	20,240	-	20,240
Dividends	-	-	(11,250)	-	(11,250)
Transfer to statutory reserves	-	696	(696)	-	-
Transfer to legal reserves	1,012	-	(1,012)	-	-
As at 31 December 2016	**15,260**	**214,053**	**25,238**	**49**	**254,600**

Legal reserves

In accordance with the Articles of Association of Banka Koper d.d., the Bank forms legal reserves in the amount adequate to ensure that the sum of its legal reserves and those capital reserves that shall be added to the legal reserves pursuant to the law governing the required amount of legal reserves equals twice the amount of the Bank’s share capital.

Statutory reserves

The Bank, according to its Statute, creates statutory reserves until they achieve an amount which is fifteen times that of the Bank's registered capital stock. In each financial year, a part of the net profit that remained after any losses carried forward, legal reserves and reserves for own shares have been covered, can be allocated to statutory reserves.

41. DIVIDENDS PER SHARE

Dividends payable are not accounted for until they have been ratified by the Annual General Meeting. By the date the financial statements were authorised by the Management Board no dividends were proposed or declared. For 2015, the Bank disbursed for dividends EUR 11,250 thousand i.e. EUR 21,21 per share.

(in thousands of euros)

Distribution of the profit of the year	2016	2015
Net profit for the period	20,240	11,843
Allocation of the profit to the legal reserves (5%)	(1,012)	(593)
Net profit of the period available for distribution	**19,228**	**11,250**
Retained profit from Finor Leasing's merger	-	697
Total net profit available for distribution at the AGM	**19,228**	**11,947**

42. CASH AND CASH EQUIVALENTS

(in thousands of euros)

	2016	2015
Cash and balances with central bank	175,394	218,046
Loans and advances to banks	15,968	46,407
Total	**191,362**	**264,453**

The figure Cash and balances with central bank differs from those in Statement of financial position due to mandatory reserve liability to central bank (note 19).

43. CONTINGENT LIABILITIES AND COMMITMENTS

Capital commitments, At 31 December 2016, the Bank had no capital commitments (2015: nil).

Credit related commitments, Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, are exposed to credit risk, as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorising a third party draw funds from the Bank up to a stipulated amount under specific terms and conditions, are secured by the underlying shipments of goods to which they relate and therefore have significantly less risk, also because the Bank do not generally expect the third party to draw funds under such agreements.

With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to losses in an amount equal to the total unused commitments. However, the likely amount of losses is not easy to quantify and is considerably less than the total unused commitments since most commitments to extend credit are contingent upon customers fulfilment of specific credit standards which need to be met before the carrying out of the drawing. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

The following table indicates the contractual amounts of the Bank's off-balance sheet position by type of instrument.

(in thousands of euros)

	2016	2015
Documentary and commercial letters of credit	160	160
Guarantees	179,948	176,597
Credit commitments:	281,811	305,629
- original maturity up to 1 year	113,835	222,186
- original maturity over 1 year	167,976	83,443
	461,919	**482,386**
Provisions for off-balance sheet liabilities:		
Guarantees	(3,610)	(3,892)
Credit commitments	(1,043)	(2,622)
Total	**457,266**	**475,872**

44. RELATED PARTY TRANSACTIONS

(in thousands of euros)

	Directors and employees with managerial contract		Management board and their direct family members		Supervisory board members and their direct family members		Intesa SanPaolo group	
	2016	2015	2016	2015	2016	2015	2016	2015
Loans								
At beginning of the year	174	228	72	80	-	-	141,756	174,218
Loans issued during the year	17	12	-	80	-	-	1,989,330	1,185,330
Loan repayments during the year	(62)	(66)	(7)	(88)	-	-	(2,053,369)	(1,217,792)
At end of year	**129**	**174**	**65**	**72**	**-**	**-**	**77,717**	**141,756**
Impairment as at 31 December	-	-	-	-	-	-	-	-
Collateral received as at 31 December	487	548	269	285	-	-	-	-
Deposits								
At beginning of the year	737	818	2,452	2,512	141	243	79,768	80,906
Deposits received during the year	2,813	2,374	10,005	9,380	693	421	98,284	62,293
Deposits repaid during the year	(2,657)	(2,455)	(9,944)	(9,440)	(707)	(523)	(61,869)	(63,431)
At end of year	**893**	**737**	**2,513**	**2,452**	**127**	**141**	**116,183**	**79,768**
Interest expense on deposits	6	33	21	88	1	16	1,627	1,549
Interest income earned	4	11	1	2	-	-	222	298
Other revenue – fee income	1	1	1	2	-	1	285	269
Guarantees issued by the bank and commitments	-	-	-	-	-	-	1,993	4,902
Remuneration	**985**	**911**	**2,131***	**2,133**	**79***	**76**		

There were no transactions made with companies in which the Management board, Supervisory board members and their closer family members or employees with managerial contract had significant influence.

* Listed by names:

(in thousands of euros)

Management board	Gross salary	Bonuses	Other	Payments under pension plan	Total
Giancarlo Miranda	369	145	14	-	528
Igor Kragelj	284	26	4	3	317
Aleksander Lozej	195	30	3	3	231
Aleksander Milostnik	194	31	4	3	232
Rado Grdina	204	31	9	3	247
Irena Džaković	199	31	13	3	246
Maurizio Marson	231	43	56	-	330
Total	**1,676**	**337**	**103**	**15**	**2,131**

(in thousands of euros)

Supervisory board members	Attendance fee	Bonuses	Total
Vojko Čok (member until 19.12.2016)	4	27	31
Roberto Civalleri	3	20	23
Borut Bratina	5	20	25
Uroš Čufer (member from 19.12.2016)	-	-	-
Total	**12**	**67**	**79**

45. EVENTS AFTER THE REPORTING PERIOD

Consistent with the Intesa Sanpaolo Group's international strategies ensuing from the 2014-17 business plan the Board of Directors of the Intesa Sanpaolo Group has taken the decision to enhance the Group's presence in Slovenia.

Leveraging on its own specific competencies and best practice, earned throughout the 15 years of the Intesa Sanpaolo's Group presence in Slovenia, Banka Koper will undertake a comprehensive business enhancement initiative. One of the pillars which this growth-propelling initiative is built on represents a change of the Bank's name to Intesa Sanpaolo Bank, a sign of the Group's commitment to serve Slovene customers nationwide, with the best international standards for banking services and products.

A decision to change the Bank's registered name to Banka Intesa Sanpaolo d.d. (Intesa Sanpaolo Bank for commercial use as a brand) was adopted at the General Assembly on 19 December 2016, to come into effect on 16 January 2017. At the same time, the shareholders took also a decision to appoint Uroš Čufer as a new member of the Supervisory Board, who has been elected Chairman a day after, by replacing Vojko Čok as a long-time Chairman of Supervisory Board.

GALLERIE D'ITALIA.
THREE MUSEUM CENTRES: A CULTURAL NETWORK FOR THE COUNTRY.

Through the Gallerie d'Italia project, Intesa Sanpaolo intends to share its artistic and architectural heritage with the public at large: 1,000 works of art displayed in historic palazzi in three cities, forging the links in a museum network that is unique of its kind. In an architectural complex of great value, the Gallerie di Piazza Scala in Milan host a selection of two hundred nineteenth-century works of the Lombard school, along with a display itinerary dedicated to Italian art of the twentieth century. The Gallerie di Palazzo Leoni Montanari in Vicenza display the most important collection of Russian icons in the West, examples of eighteenth-century Veneto art and a collection of ceramics from Attica and Magna Graecia. In Naples, the Gallerie di Palazzo Zevallos Stigliano present the Martyrdom of Saint Ursula, one of Caravaggio's last masterpieces, along with works of southern Italian art ranging from the seventeenth to the early twentieth century.

Van Lint's view of the Church of Santa Maria della Salute with Punta della Dogana belongs to the Intesa Sanpaolo's 18th century Venetian art collection, which is part of the permanent exhibition at Gallerie d'Italia - Palazzo Leoni Montanari, the Bank's museum venue in Vicenza. The collection offers a review of all the pictorial genres - particularly landscape painting - that won Venice and its school a central role on the international artistic scene in the 18th century. Views of many Italian locations, including Venice, painted by Gaspar van Wittel (late 1600s) were crucial for the success met by this genre in the 1700s. Among his main followers, we cannot fail to mention Hendrik Frans van Lint, a famous Flemish painter who was much sought after for the extreme refinement of his works.

Cover photo:

HENDRIK FRANS VAN LINT
(Antwerp, 1684 - Rome, 1763)
Church of Santa Maria della Salute with Punta della Dogana, *ca. 1750*
Oil on canvas, 46.5 x 71.5 cm
Intesa Sanpaolo Collection
Gallerie d'Italia - Palazzo Leoni Montanari, Vicenza

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