BANCA INTESA
(JOINT-STOCK COMPANY)

Consolidated financial statements

Year ended 31 December 2017
Together with Independent Auditors' Report

Contents

Independent Auditors' Report

To the Shareholders and Board of Directors of BANCA INTESA (JOINT-STOCK COMPANY)

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of BANCA INTESA (JOINT-STOCK COMPANY) (the "Bank") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2017, the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

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 *Auditors' Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the independence requirements that are relevant to our audit of the consolidated financial statements in the Russian Federation and with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the requirements in the Russian Federation and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Audited entity: BANCA INTESA (JOINT-STOCK COMPNAY)

Registration No. in the Unified State Register of Legal Entities 1027739177377.

Moscow, the Russian Federation

Independent auditor: JSC "KPMG", a company incorporated under the Laws of the Russian Federation, a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.

Registration No. in the Unified State Register of Legal Entities 1027700125628.

Member of the Self-regulated organisation of auditors "Russian Union of auditors" (Association). The Principal Registration Number of the Entry in the Register of Auditors and Audit Organisations: No. 11603053203.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Impairment of loans to customers

Please refer to Notes 8 and 25 in the consolidated financial statements.

The key audit matter	How the matter was addressed in our audit
The impairment of loans to customers is estimated by the Group through the application of judgment and use of subjective assumptions. Due to the significance of loans to customers (representing 53% of total assets) and the related estimation uncertainty, this is considered to be a key audit matter. We paid particular attention to assumptions and methodology used for calculation of impairment allowance for loans to legal entities with individual indicators of impairment. We also focused on the methodology used to calculate collective impairment allowance for loans to legal entities without individual indicators of impairment.	We assessed and tested the design and operating effectiveness of the controls over impairment calculation. Where impairment is calculated collectively for portfolios of loans, based on historic data, we assessed whether historic experience was reflective of the losses incurred in the portfolios based upon the current economic environment and the current circumstances of the borrowers by comparing historical information to our own assessment. We assessed and tested the design and operating effectiveness of the controls over the transition of data related to impairment calculation between accounting and risk-management systems involving our internal IT specialists. For a sample of exposures that were subject to an individual impairment assessment, and focusing on those with the most significant potential impact on the consolidated financial statements, we specifically challenged the Group's assumptions on the expected future cash flows, including the value of realisable collateral based on our own understanding and available market information. We also assessed whether the consolidated financial statement disclosures appropriately reflect the Group's exposure to credit risk.

Other Information

Management is responsible for the other information. The other information comprises the information included in the Annual report for the year ended 31 December 2017 but does not include the consolidated financial statements and our auditors' report thereon. The Annual report is expected to be made available to us after the date of this auditors' report.

Our opinion on the consolidated financial statements does not cover the other information and we will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

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

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

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated 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 consolidated financial statements.

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

— Identify and assess the risks of material misstatement of the consolidated 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 Group'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 Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated 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 Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report of findings from procedures performed in accordance with the requirements of Federal Law No. 395-1, dated 2 December 1990, *On Banks and Banking Activity*

Management is responsible for the Group's compliance with mandatory ratios and for maintaining internal control and organising risk management systems in accordance with requirements established by the Bank of Russia.

In accordance with Article 42 of Federal Law No. 395-1, dated 2 December 1990, *On Banks and Banking Activity* (the "Federal Law"), we have performed procedures to examine:

- the Group's compliance with mandatory ratios as at 1 January 2018 established by the Bank of Russia; and
- whether the elements of the Group's internal control and organisation of its risk

management systems comply with the requirements established by the Bank of Russia.

These procedures were selected based on our judgment and were limited to the analysis, inspection of documents, comparison of the Bank's internal policies, procedures and methodologies with the applicable requirements established by the Bank of Russia, and recalculations, comparisons and reconciliations of numerical data and other information.

Our findings from the procedures performed are reported below.

— Based on our procedures with respect to the Group's compliance with the mandatory ratios established by the Bank of Russia, we found that the Group's mandatory ratios as at 1 January 2018 were within the limits established by the Bank of Russia.

  We have not performed any procedures on the accounting records maintained by the Group other than those which we considered necessary to enable us to express an opinion as to whether the Group's consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with the International Financial Reporting Standards.

— Based on our procedures with respect to whether the elements of the Group's internal control and organisation of its risk management systems comply with the requirements established by the Bank of Russia, we found that:

  - as at 31 December 2017, the Bank's Internal Audit function was subordinated to, and reported to, the Board of Directors, and the Risk Management function was not subordinated to, and did not report to, divisions taking relevant risks in accordance with regulations and recommendations issued by the Bank of Russia;

  - the Bank's internal documentation, effective on 31 December 2017, establishing the procedures and methodologies for identifying and managing the Group's significant credit, operational, market, interest rate, legal, liquidity and reputational risks, and for stress-testing was approved by the authorised management bodies of the Bank in accordance with the regulations and recommendations issued by the Bank of Russia;

  - as at 31 December 2017, the Bank maintained a system for reporting on the Group's significant credit, operational, market, interest rate, legal, liquidity and reputational risks, and on the Group's capital;

  - the frequency and consistency of reports prepared by the Bank's Risk Management and Internal Audit functions during 2017, which cover the Group's credit, operational, market, interest rate, legal, liquidity and reputational risk management, was in compliance with the Bank's internal documentation. The reports included observations made by the Bank's Risk Management and Internal Audit functions as to their assessment of the effectiveness of the Bank's procedures and methodologies, and recommendations for improvement;

  - as at 31 December 2017, the Board of Directors and the Management Board of the Bank had responsibility for monitoring the Group's compliance with the risk limits and capital adequacy ratios established in the Bank's internal documentation. In order to monitor the effectiveness of the Group's risk management procedures and their consistent application during 2017 the Board of Directors and the Management Board of the Bank periodically discussed reports prepared by the Risk Management and Internal Audit functions, and considered the proposed corrective actions.

Procedures with respect to elements of the Group's internal control and organisation of its risk management systems were performed solely for the purpose of examining whether these elements, as prescribed in the Federal Law and as described above, comply with the requirements established by the Bank of Russia.

The engagement partner on the audit resulting in this independent auditors' report is:

Shevarenkov Evgeny Victorovich

JSC "KPMG"

Moscow, the Russian Federation

19 February 2018

Consolidated statement of financial position

As at 31 December 2017

(Thousands of Russian Roubles)

	Notes	*2017*	*2016*
Assets			
Cash and cash equivalents	4	3 886 295	3 918 233
Mandatory cash balances with the Central Bank of the Russian Federation		298 979	268 738
Amounts due from credit institutions	5	13 528 737	12 237 918
Available-for-sale securities:			
- held by the Bank	6	4 130 899	3 535 812
Derivative financial assets	7	-	1 735
Loans to customers:		28 995 088	30 537 651
- loans to large corporate customers	*8*	*12 950 962*	*13 370 206*
- loans to small and medium corporate customers	*8*	*14 282 671*	*15 569 469*
- loans to retail customers	*8*	*1 761 455*	*1 597 976*
Net investments in finance leases	9	1 334 117	998 177
Property and equipment	11	1 131 217	696 643
Intangible assets	12	585 667	720 572
Deferred income tax assets	13	328 348	626 732
Other assets	15	874 403	1 385 103
Total assets		**55 093 750**	**54 927 314**
Liabilities			
Amounts due to credit institutions	16	5 884 650	6 860 745
Derivative financial liabilities	7	-	786
Amounts due to customers:		30 527 105	27 965 071
- legal entities, state and non-profit organisations	*17*	*13 700 703*	*18 487 613*
- individuals	*17*	*16 826 402*	*9 477 458*
Debt securities issued	18	3 186 066	4 875 106
Other liabilities	15	746 512	741 503
Subordinated debt	19	2 304 839	2 426 712
Total liabilities		**42 649 172**	**42 869 923**
Equity	20		
Share capital		10 820 181	10 820 181
Other capital reserve		1 803 914	1 803 914
Revaluation reserve for available-for-sale securities		22 802	21 830
Revaluation of premises		384 144	-
Accumulated losses		(586 463)	(588 534)
Total equity		**12 444 578**	**12 057 391**
Total equity and liabilities		**55 093 750**	**54 927 314**

Signed and authorised for release on behalf of the Management Board of the Bank

Gianluca Corrias — Chairman of the Management Board

Tatyana Pavlycheva — Member of the Management Board/Head of Accounting, Planning and Control Group/Chief accountant

19 February 2018

The accompanying Notes are an integral part of these consolidated financial statements.

Consolidated statement of profit or loss and other comprehensive income

For the year ended 31 December 2017

(Thousands of Russian Roubles)

	Notes	*2017*	*2016*
Interest income			
Loans to customers		3 986 434	5 650 856
Amounts due from credit institutions		606 401	491 356
Available-for-sale securities		336 723	308 206
Net investments in finance leases		230 026	232 409
		5 159 584	**6 682 827**
Interest expense			
Amounts due to customers		(1 267 902)	(1 496 830)
Debt securities issued		(391 791)	(463 045)
Amounts due to credit institutions		(265 796)	(741 206)
Subordinated debt		(153 585)	(176 436)
		(2 079 074)	**(2 877 517)**
Net interest income		**3 080 510**	**3 805 310**
Impairment of loans, net investments in finance leases and amounts due from credit institutions	10	(319 952)	(953 745)
Net interest income after impairment of loans, net investments in finance leases and amounts due from credit institutions		**2 760 558**	**2 851 565**
Fee and commission income		1 015 654	1 582 010
Fee and commission expense		(145 278)	(161 046)
Net fee and commission income	22	**870 376**	**1 420 964**
Net gains from available-for-sale securities		6 139	5 559
Net gains from foreign currencies:			
- dealing		(161 415)	793 213
- translation differences		395 958	(790 608)
Net losses from other operating activities	23	(68 707)	(96 250)
Operating income		**3 802 909**	**4 184 443**
Personnel expenses	24	(1 709 822)	(1 828 367)
Other general administrative expenses	24	(1 267 204)	(1 476 949)
Depreciation and amortisation	11, 12	(439 457)	(382 707)
Other impairment and provisions	14	(108 847)	(45 521)
Profit before income tax		**277 579**	**450 899**
Income tax expense	13	(275 508)	(93 439)
Profit for the year		**2 071**	**357 460**
Other comprehensive income, net of income tax			
Items that are or may be reclassified subsequently to profit or loss:			
Revaluation reserve for available-for-sale financial assets:			
- Net change in fair value of available-for-sale securities		6 127	11 826
- Net change in fair value of available-for-sale securities transferred to profit or loss		(5 155)	26
Total items that are or may be reclassified subsequently to profit or loss		*972*	*11 852*
Items that will not be reclassified to profit or loss:			
Revaluation of premises	11	384 144	-
Total items that will not reclassified to profit or loss		*384 144*	-
Total other comprehensive income for the year, net of income tax		**385 116**	**11 852**
Total comprehensive income for the year		**387 187**	**369 312**

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19 February 2018

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Consolidated statement of changes in equity

For the year ended 31 December 2017

(Thousands of Russian Roubles)

	Share capital	*Other capital reserve*	*Revaluation reserve for available-for-sale securities*	*Revaluation of premises*	*Retained earnings (accumulated losses)*	*Total equity*
Balance as at 1 January 2016	**10 820 181**	**1 803 914**	**9 978**	–	**(945 994)**	**11 688 079**
Total comprehensive income						
Profit for the year	–	–	–	–	357 460	**357 460**
Other comprehensive income						
Items that are or may be reclassified subsequently to profit or loss:						
Net change in fair value of available-for-sale securities, net of deferred tax of RUB 2 957 thousand	–	–	11 826	–	–	**11 826**
Net change in fair value of available-for-sale securities transferred to profit or loss, net of deferred tax of RUB 6 thousand	–	–	26	–	–	**26**
Total items that are or may be reclassified subsequently to profit or loss	–	–	*11 852*	–	–	***11 852***
Total other comprehensive income	–	–	11 852	–	–	**11 852**
Total comprehensive income for the year	–	–	11 852	–	357 460	**369 312**
Balance as at 31 December 2016	**10 820 181**	**1 803 914**	**21 830**	–	**(588 534)**	**12 057 391**
Total comprehensive income						
Profit for the year	–	–	–	–	2 071	**2 071**
Other comprehensive income						
Items that are or may be reclassified subsequently to profit or loss:						
Net change in fair value of available-for-sale securities, net of deferred tax of RUB 1 533 thousand	–	–	6 127	–	–	**6 127**
Net change in fair value of available-for-sale securities transferred to profit or loss, net of deferred tax of RUB 1 289 thousand	–	–	(5 155)	–	–	**(5 155)**
Total items that are or may be reclassified subsequently to profit or loss	–	–	*972*	–	–	*972*
Items that will not be reclassified to profit or loss:						
Revaluation of premises, net of deferred tax of RUB 96 036 thousand	–	–	–	384 144	–	**384 144**
Total items that will not be reclassified to profit or loss	–	–	–	*384 144*	–	***384 144***
Total other comprehensive income	–	–	972	384 144	–	**385 116**
Total comprehensive income for the year	–	–	972	384 144	2 071	**387 187**
Balance as at 31 December 2017	**10 820 181**	**1 803 914**	**22 802**	**384 144**	**(586 463)**	**12 444 578**

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19 February 2018

The accompanying Notes are an integral part of these consolidated financial statements.

Consolidated statement of cash flows

For the year ended 31 December 2017

(Thousands of Russian Roubles)

	Note	2017	2016
Cash flows from operating activities			
Interest received		4 866 618	6 606 858
Interest paid		(2 388 949)	(2 812 350)
Fees and commissions received		1 569 628	1 029 791
Fees and commissions paid		(149 310)	(158 928)
Net (payments) receipts from dealing in foreign currencies		(160 467)	750 380
Net payments for other operating activities		(48 044)	(76 108)
Personnel expenses paid		(1 704 220)	(1 818 461)
Other general administrative expenses paid		(1 180 197)	(1 533 281)
Cash flows from operating activities before changes in operating assets and liabilities		**805 059**	**1 987 901**
Net (increase) decrease in operating assets			
Mandatory cash balances with the Central Bank of the Russian Federation		(30 241)	(74 783)
Amounts due from credit institutions		(1 031 031)	(4 597 156)
Loans to customers		1 294 658	10 901 255
Net investments in finance leases		(334 484)	60 116
Other assets		130 939	1 153 851
Net (decrease) increase in operating liabilities			
Amounts due to credit institutions		(833 139)	(11 923 210)
Amounts due to customers		2 585 060	764 435
Other liabilities		(49 783)	31 297
Net cash provided from (used in) operating activities before income tax paid		**2 537 038**	**(1 696 294)**
Income tax paid		(79 895)	(29 937)
Net cash flows provided from (used in) operating activities		**2 457 143**	**(1 726 231)**
Cash flows from investing activities			
Purchase of property and equipment		(196 722)	(403 591)
Proceeds from sale of property and equipment		667	570
Purchase of intangible assets		(154 446)	(446 951)
Purchase of available-for-sale securities		(3 586 878)	(1 669 588)
Proceeds from sale and redemption of available-for-sale securities		3 034 630	742 571
Net cash flows used in investing activities		**(902 749)**	**(1 776 989)**
Cash flows from financing activities			
Proceeds from debt securities issued	19	-	3 350 000
Repayment of debt securities issued	19	(1 686 508)	(3 532 849)
Net cash flows used in financing activities		**(1 686 508)**	**(182 849)**
Effect of exchange rates changes on cash and cash equivalents		100 176	(1 549 552)
Net decrease in cash and cash equivalents		**(31 938)**	**(5 235 621)**
Cash and cash equivalents as at the beginning of the year	4	3 918 233	9 153 854
Cash and cash equivalents as at the end of the year	4	**3 886 295**	**3 918 233**

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Gianluca Corrias — Chairman of the Management Board

Tatyana Pavlycheva — Member of the Management Board/Head of Accounting, Planning and Control Group/Chief accountant

19 February 2018

The accompanying Notes are an integral part of these consolidated financial statements.

(Thousands of Russian Roubles)

1. Principal activities

These consolidated financial statements include the financial statements of Banca Intesa (Joint-Stock Company) and its subsidiary, AO “Intesa Leasing”, together referred to as the “Bank”.

Banca Intesa (Joint-Stock Company) is a commercial bank organised in the form of a joint-stock company under the laws of the Russian Federation.

The Bank, formerly known as KMB Bank (Closed Joint-Stock Company) (the “incorporating Bank”), changed its name following the merger with ZAO Banca Intesa (the “incorporated Bank”), 100% Russian banking subsidiary of Intesa Sanpaolo S.p.A. (Italy), on 11 January 2010.

The shareholders of the Bank as at 31 December are:

Shareholder	***2017*** ***%***	***2016*** ***%***
Intesa Sanpaolo S.p.A. (Italy)	46.9772	46.9772
Intesa Sanpaolo Holding International SA (Luxembourg)	53.0228	53.0228
Total	100.0000	100.0000

The ultimate controlling party of the Bank is Intesa Sanpaolo S.p.A. (Italy) (“ISP”).

The Bank’s principal business activities are corporate banking products to small, medium and large businesses and retail banking products and services, including a premium banking segment. The Bank is engaged in a program of the Corporation MSP, the Ministry of Economic Development of the Russian Federation and the Central Bank of the Russian Federation (the “CBR”) to support the businesses of small to medium sized companies by providing them with lending facilities.

The activities of the Bank are regulated by the CBR. The Bank operates under General Banking License № 2216.

In 2004, the Bank became a member of the state deposit insurance system in the Russian Federation.

The Bank has a wholly owned and controlled subsidiary, AO “Intesa Leasing”, former ZAO “KMB-Leasing”. It is primarily engaged in the provision of finance leases to the Bank’s clients and other companies.

The Bank’s head office is located in Moscow and it has 6 branches within the Russian Federation in the cities of Saint Petersburg, Nizhniy Novgorod, Ekaterinburg, Novosibirsk, Vladivostok and Rostov-on-Don (2016: 6 branches). As at 31 December 2017, the Bank has 37 offices selling banking products in different cities within the Russian Federation (2016: 36 offices). No offices were closed during year ended 31 December 2017 (2016: 14 offices) in course of network optimisation.

The Bank’s registered office is located at the following address: 2, Petroverigsky pereulok, Moscow, Russian Federation, 101000.

As at 31 December 2017, the Bank employed 1 384 people (2016: 1 463).

Russian business environment

The Bank’s operations are primarily located in the Russian Federation. Consequently, the Bank is exposed to the economic and financial markets of the Russian Federation which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in the Russian Federation.

The conflict in Ukraine and related events has increased the perceived risks of doing business in the Russian Federation. The imposition of economic sanctions on Russian individuals and legal entities by the European Union, the United States of America, Japan, Canada, Australia and others, as well as retaliatory sanctions imposed by the Russian government, has resulted in increased economic uncertainty including more volatile equity markets, a fluctuation of the Russian Rouble, a reduction in both local and foreign direct investment inflows and a significant tightening in the availability of credit. In particular, some Russian entities may be experiencing difficulties in accessing international equity and debt markets and may become increasingly dependent on Russian state banks to finance their operations. The longer term effects of recently implemented sanctions, as well as the threat of additional future sanctions, are difficult to determine.

The consolidated financial statements reflect management’s assessment of the impact of the Russian business environment on the operations and financial position of the Bank. The future business environment may differ from management’s assessment.

(Thousands of Russian Roubles)

2. Basis of preparation

Statement of compliance

The accompanying consolidated financial statements are prepared in accordance with International Financial Reporting Standards (“IFRS”).

The Bank is required to maintain its records and prepare its financial statements for regulatory purposes in Russian Roubles in accordance with the Russian accounting and banking legislation and related instructions (“RAL”). These consolidated financial statements are based on the Bank’s RAL books and records, as adjusted and reclassified in order to comply with IFRS.

Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except for available-for-sale securities and derivative financial instruments that are stated at fair value.

Functional and presentation currency

The functional currency of the Bank and its subsidiary is the Russian Rouble (“RUB”) as, being the national currency of the Russian Federation, it reflects the economic substance of the majority of underlying events and circumstances relevant to them.

The RUB is also the presentation currency for the purposes of these consolidated financial statements.

All financial information presented in RUB is rounded to the nearest thousand, except where indicated.

Use of estimates and judgments

The preparation of these consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Although these estimates are based on management’s best knowledge of current events and actions, actual results ultimately may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies is described in the following notes:

- loan impairment estimates – Note 8 and Note 25;
- net investments in finance leases impairment estimates – Note 9;
- premises revaluation estimates – Note 11;
- tax contingency estimates – Note 21;
- estimates of fair values of financial instruments – Note 26;
- repossessed collateral – Note 26.

Changes in accounting policies and presentation

As at 31 December 2017, the Bank has changed its accounting policy for premises category within property and equipment, adopting the revaluation model instead of the cost model. The change from a cost model to a revaluation model is accounted for as a revaluation in accordance with IAS 16 *Property, Plant and Equipment*, and therefore is accounted for prospectively. In the management’s assessment the change from a cost model to a revaluation model will provide a more relevant presentation of financial information.

The Bank has adopted the following amendments to standards with a date of initial application of 1 January 2017:

- *Disclosure Initiative (Amendments to IAS 7).* IAS 7 *Statement of Cash Flows* has been amended as part of the IASB’s broader disclosure initiative to improve presentation and disclosure in financial statements. The amendment requires disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes. One way to meet this new disclosure requirement is to provide a reconciliation between the opening and closing balances for liabilities arising from financing activities. However, the objective could also be achieved in other ways.
- *Recognition of Deferred Tax Asset for Unrealised Losses (Amendments to IAS 12).* The amendments to IAS 12 *Income Taxes* clarify that the existence of a deductible temporary difference depends solely on a comparison of

(Thousands of Russian Roubles)

the carrying amount of an asset and its tax base at the end of the reporting period, and is not affected by possible future changes in the carrying amount or expected manner of recovery of the asset. Therefore, assuming that the tax base remains at the original cost of the debt instrument, there is a temporary difference. The amendments show that the entity can recognise a deferred tax asset if the future bottom line of its tax return is expected to be a loss if certain conditions are met.

- *Annual Improvements to IFRSs 2014–2016 Cycle – various standards (Amendments to IFRS 12).* Amendments to IFRS 12 *Disclosure of Interests in Other Entities* clarify that the disclosure requirements for interests in other entities also apply to interests that are classified as held for sale or distribution.

3. Summary of accounting policies

The following accounting policies are consistently applied in the preparation of the consolidated financial statements, except as explained in Note 2, which addresses changes in accounting policies.

Basis of consolidation

Business combinations

Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Bank.

The Bank measures goodwill at the acquisition date as the fair value of the consideration transferred (including the fair value of any previously-held equity interest in the acquiree if the business combination is achieved in stages) and the recognised amount of any non-controlling interest in the acquiree, less the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed. When the excess is negative, a bargain purchase gain is recognised immediately in profit or loss.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Any contingent consideration payable is measured at fair value at the acquisition date. If the contingent consideration is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

The Bank elects on transaction-by-transaction basis whether to measure non-controlling interests at fair value, or at their proportionate share of the recognised amount of the identifiable net assets of the acquiree, at the acquisition date.

Transaction costs, other than those associated with the issue of debt or equity securities, that the Bank incurs in connection with a business combination are expensed as incurred.

Subsidiaries

Subsidiaries are investees controlled by the Bank. The Bank controls an investee when it is exposed to, or has rights to, variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. In particular the Bank consolidates investees that it controls on the basis of de facto circumstances. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Acquisitions and disposals of non-controlling interests

The Bank accounts for the acquisitions and disposals of non-controlling interests as transactions with equity holders in their capacity as equity holders. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the parent.

Foreign currency transactions

Transactions in foreign currencies are translated to the functional currency of the Bank at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period. Foreign currency differences arising on retranslation are recognised in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments unless the difference is due to impairment in which case foreign currency differences that have been recognised in other comprehensive income are reclassified to profit or loss; a financial liability designated as a hedge of the net investment in a foreign operation to the extent that the hedge is effective; or qualifying cash flow hedges to the extent that the hedge is effective, which are recognised in other comprehensive income.

(Thousands of Russian Roubles)

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the CBR, excluding mandatory cash balances with the CBR, and accounts which can be converted into cash within one day and are free from contractual encumbrances. All short-term interbank placements are included in amounts due from other banks. Cash and cash equivalents are carried at amortised cost in the consolidated statement of financial position.

Mandatory cash balances with the CBR

Credit institutions are required to maintain a non-interest earning cash deposit (mandatory cash balances) with the CBR, the amount of which depends on the level of funds attracted by the credit institution. The Bank's ability to withdraw such a deposit is significantly restricted by the statutory legislation. Mandatory cash balances with the CBR are not available to finance the Bank's day-to-day operations and hence are not considered as part of cash and cash equivalents for the purposes of the consolidated statement of cash flows.

Financial instruments

Classification

Financial instruments at fair value through profit or loss are financial assets or liabilities that are:

- acquired or incurred principally for the purpose of selling or repurchasing in the near term;

- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking;

- derivative financial instruments (except for derivative that is a financial guarantee contract or a designated and effective hedging instruments) or,

- upon initial recognition, designated as at fair value through profit or loss.

The Bank may designate financial assets and liabilities at fair value through profit or loss where either:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis;

- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise or,

- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported as assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported as liabilities.

Management determines the appropriate classification of financial instruments in this category at the time of the initial recognition. Derivative financial instruments and financial instruments designated as at fair value through profit or loss upon initial recognition are not reclassified out of at fair value through profit or loss category.

Financial assets that would have met the definition of loans and receivables may be reclassified out of the fair value through profit or loss or available-for-sale category if the Bank has an intention and ability to hold them for the foreseeable future or until maturity. Other financial instruments may be reclassified out of at fair value through profit or loss category only in rare circumstances. Rare circumstances arise from a single event that is unusual and highly unlikely to recur in the near term.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Bank:

- intends to sell immediately or in the near term;

- upon initial recognition designates as at fair value through profit or loss;

- upon initial recognition designates as available-for-sale or,

- may not recover substantially all of its initial investment, other than because of credit deterioration.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and ability to hold to maturity, other than those that:

- the Bank upon initial recognition designates as at fair value through profit or loss;

- the Bank designates as available-for-sale or,

- meet the definition of loans and receivables.

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

(Thousands of Russian Roubles)

Recognition

Financial assets and liabilities are recognised in the consolidated statement of financial position when the Bank becomes a party to the contractual provisions of the instrument. All regular way purchases of financial assets are accounted for at the settlement date.

Measurement

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets, including derivatives that are assets, are measured at their fair values, without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

- loans and receivables which are measured at amortised cost using the effective interest method;

- held-to-maturity investments that are measured at amortised cost using the effective interest method;

- investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured which are measured at cost.

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortised cost.

'Day 1' profit

Where the transaction price in a non-active market is different from the fair value from other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets, the Bank immediately recognises the difference between the transaction price and fair value (a 'Day 1' profit) in the consolidated statement of profit or loss and other comprehensive income. In cases where data used is not observable, the difference between the transaction price and model value is only recognised in the consolidated statement of profit or loss and other comprehensive income when the inputs become observable, or when the instrument is derecognised.

Amortised cost

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

Fair value measurement principles

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

When there is no quoted price in an active market, the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all the factors that market participants would take into account in pricing transaction.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price, i.e., the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is supported wholly by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, the Bank measures assets and long positions at the bid price and liabilities and short positions at the ask price.

Gains and losses on subsequent measurement

A gain or loss arising from a change in the fair value of a financial asset or liability is recognised as follows:

- a gain or loss on a financial instrument classified as at fair value through profit or loss is recognised in profit or loss;

(Thousands of Russian Roubles)

- a gain or loss on an available-for-sale financial asset is recognised as other comprehensive income in equity (except for impairment losses and foreign exchange gains and losses on debt financial instruments available-for-sale) until the asset is derecognised, at which time the cumulative gain or loss previously recognised in equity is recognised in profit or loss. Interest in relation to an available-for-sale financial asset is recognised in profit or loss using the effective interest method.

For financial assets and liabilities carried at amortised cost, a gain or loss is recognised in profit or loss when the financial asset or liability is derecognised or impaired, and through the amortisation process.

Derecognition

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability in the consolidated statement of financial position. The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Bank enters into transactions whereby it transfers assets recognised on its consolidated statement of financial position, but retains either all risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised.

In transactions where the Bank neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset, it derecognises the asset if control over the asset is lost.

In transfers where control over the asset is retained, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred assets.

If the Bank purchases its own debt, it is removed from the consolidated statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains or losses arising from early retirement of debt.

The Bank writes off assets deemed to be uncollectible.

Repurchase and reverse repurchase agreements

Securities sold under sale and repurchase (“repo”) agreements are accounted for as secured financing transactions, with the securities retained in the consolidated statement of financial position and the counterparty liability included in amounts payable under repo transactions within amounts due to credit institutions or amounts due to customers, as appropriate. The difference between the sale and repurchase prices represents interest expense and is recognised in profit or loss over the term of the repo agreement using the effective interest method.

Securities purchased under agreements to resell (“reverse repo”) are recorded as amounts receivable under reverse repo transactions within due from banks or loans to customers, as appropriate. The difference between the purchase and resale prices represents interest income and is recognised in profit or loss over the term of the reverse repo agreement using the effective interest method.

If assets purchased under an agreement to resell are sold to third parties, the obligation to return securities is recorded as a trading liability and measured at fair value.

Derivative financial instruments

Derivative financial instruments include swaps, forwards, spot transactions in interest rates, foreign exchanges and any combinations of these instruments.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Changes in the fair value of derivatives are recognised immediately in profit or loss.

Offsetting

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

(Thousands of Russian Roubles)

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include amounts due to government, amounts due to credit institutions, amounts due to customers, other borrowed funds, subordinated debt and debt securities issued. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the consolidated statement of profit or loss and other comprehensive income when the borrowings are derecognised as well as through the amortisation process.

Leases

Finance - Bank as a lessor

The Bank recognises lease receivables at a value equal to the net investment in the lease, starting from the date of commencement of the lease term.

Finance income is based on a pattern reflecting a constant periodic rate of return on the net investment outstanding. Initial direct costs are included in the initial measurement of the lease receivables.

When the Bank takes possession of the collateral under terminated lease contracts, it measures the assets at the lower of net realisable value and amortised historical cost of the inventory.

Operating – Bank as a lessee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included in other operating expenses.

Property and equipment

Items of property and equipment are stated at cost, except for premises, which are stated at revalued amounts as described below.

Such cost excludes the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment losses and includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Premises are subject to revaluation on a regular basis. The frequency of revaluation depends on the movements in the fair values of the premises being revalued. A revaluation increase on a premise is recognised as other comprehensive income except to the extent that it reverses a previous revaluation decrease recognised in profit or loss, in which case it is recognised in profit or loss. A revaluation decrease on a premise is recognised in profit or loss except to the extent that it reverses a previous revaluation increase recognised as other comprehensive income directly in equity, in which case it is recognised in other comprehensive income.

Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Land is not depreciated. Depreciation is calculated on a straight-line basis (calculated by quantity of days of the corresponding month) over the following estimated useful lives of the assets using the following rates:

	per annum, %
Premises	3
Office and computer equipment	15-33
Intangible assets	20-50

The residual values of the assets, useful lives and methods are reviewed, and adjusted as appropriate, at each reporting period.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalisation.

Equipment purchased for leasing purposes

The Bank accounts for capital expenditures related to acquisition of equipment subject to leasing as equipment purchased for leasing purposes. These expenditures are accumulated until the equipment is ready for use and transferred to the lessee.

(Thousands of Russian Roubles)

Intangible assets

Intangible assets include computer software and licences.

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. Following initial recognition, intangible assets are stated at cost less accumulated amortisation and accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with a finite useful live are amortised over the useful economic live, not exceeding a period of 5 years, and assessed for impairment whenever there is an indication that the intangible asset may be impaired.

Amortisation is charged to profit or loss on a straight-line basis.

Intangible assets with an indefinite useful life are not amortised. The useful life of such assets is reviewed at each reporting period to determine whether events and circumstances continue to support an indefinite useful life assessment for such assets.

The Bank tests intangible assets with an indefinite useful life for impairment by comparing their recoverable amounts with the corresponding carrying amounts annually, and whenever there is an indication that an intangible asset may be impaired.

Intangible assets useful life of which has ended (licenses and computer software), should be written-off twice a year, in the end of the second and the fourth quarter or based on the order of IT Department.

Repossessed collateral

Repossessed collateral represents non-financial assets obtained by the Bank in the course of settlement of overdue loans. These assets are initially recognised at fair value when obtained and can be included in property and equipment, inventories or investment property or other assets depending on their nature and the Bank's intention and are subsequently remeasured and accounted for in accordance with the accounting policies for the respective categories.

Impairment of financial assets

The Bank assesses at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets is impaired. If any such evidence exists, the Bank determines the amount of any impairment loss.

A financial asset or group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a loss event) and that event (or events) has had an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, breach of loan covenants or conditions, restructuring of a financial asset or group of financial assets that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, deterioration in the value of collateral, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers in the group, or economic conditions that correlate with defaults in the group.

In addition, for an investment in an equity security available-for-sale a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

Financial assets carried at amortised cost

Financial assets carried at amortised cost consist principally of loans and other receivables (“loans and receivables”). The Bank reviews its loans and receivables to assess impairment on a regular basis.

The Bank first assesses whether objective evidence of impairment exists individually for loans and receivables that are individually significant, and individually or collectively for loans and receivables that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed loan or receivable, whether significant or not, it includes the loan or receivable in a group of loans and receivables with similar credit risk characteristics and collectively assesses them for impairment. Loans and receivables 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 of impairment.

If there is objective evidence that an impairment loss on a loan or receivable has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan or receivable and the present value of estimated future cash flows including amounts recoverable from guarantees and collateral discounted at the loan or receivable’s original effective interest rate. Contractual cash flows and historical loss experience adjusted on the basis of relevant observable data that reflect current economic conditions provide the basis for estimating expected cash flows.

In some cases the observable data required to estimate the amount of an impairment loss on a loan or receivable may be limited or no longer fully relevant to current circumstances. This may be the case when a borrower is in financial difficulties and there is little available historical data relating to similar borrowers. In such cases, the Bank uses its experience and judgment to estimate the amount of any impairment loss.

(Thousands of Russian Roubles)

All impairment losses in respect of loans and receivables are recognised in profit or loss and are only reversed if a subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

When a loan is uncollectable, it is written off against the related allowance for loan impairment. The Bank writes off a loan balance (and any related allowances for loan losses) when management determines that the loans are uncollectible and when all necessary steps to collect the loan are completed.

Financial assets carried at cost

Financial assets carried at cost include unquoted equity instruments included in available-for-sale financial assets that are not carried at fair value because their fair value cannot be reliably measured. If there is objective evidence that such investments are impaired, the impairment loss is calculated as the difference between the carrying amount of the investment and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset.

All impairment losses in respect of these investments are recognised in profit or loss and cannot be reversed.

Available-for-sale financial assets

Impairment losses on available-for-sale financial assets are recognised by transferring the cumulative loss that is recognised in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security 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, with the amount of the reversal recognised in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

Non financial assets

Other non financial assets, other than deferred taxes, are assessed at each reporting date for any indications of impairment. The recoverable amount of goodwill is estimated at each reporting date. The recoverable amount of non financial assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is recognised when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

All impairment losses in respect of non financial assets are recognised in profit or loss and reversed only if there has been a change in the estimates used to determine the recoverable amount. Any impairment loss reversed is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Provisions

A provision is recognised in the consolidated statement of financial position when the Bank has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

Contingencies and credit related commitments

Contingent liabilities are not recognised in the consolidated statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the consolidated statement of financial position but disclosed when an inflow of economic benefits is probable.

In the normal course of business, the Bank enters into credit related commitments including undrawn loan commitments, guarantees and letters of credit. Guarantees are initially recognised in the consolidated statement of financial position at fair value net of associated transaction costs within other liabilities, and subsequently are measured at the higher of the amortised premium or the amount of provision for losses under the guarantee.

Provisions are recognised against credit related commitments when losses are considered probable and can be measured reliably.

Any increase in the liability relating to credit related commitments is recognised in profit or loss. The premium received is recognised in profit or loss on a straight-line basis over the life of the guarantee.

(Thousands of Russian Roubles)

Retirement and other employee benefit obligations

The Bank does not have any pension arrangements other than with the State pension system of the Russian Federation, which requires current contributions by the employer calculated as a percentage of current gross salary payments; such expense is charged in the period the related salaries are earned. The Bank has no significant post-retirement benefits to its employees.

Share capital

Ordinary shares

Ordinary shares are classified as equity. Incremental costs directly attributable to the issuance of new shares, other than on a business combination, are recognised as a deduction from equity, net of any tax effects.

Share premium

Share premium represents the excess of contributions over the nominal value of the shares issued.

Other capital reserve

Funds provided by the Bank's shareholders in the form of debt free financing are classified as other capital reserves.

Dividends

The ability of the Bank to declare and pay dividends is subject to the rules and regulations of the Russian legislation.

Dividends in relation to ordinary shares are reflected as an appropriation of retained earnings in the period when they are declared.

Taxation

The current income tax expense is calculated in accordance with the regulations of the Russian Federation.

Income tax comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items of other comprehensive income or transactions with shareholders recognised directly in equity, in which case it is recognised within other comprehensive income or directly within equity.

Current tax expense is the expected tax payable on the taxable profit for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of goodwill not deductible for tax purposes, the initial recognition of assets or liabilities in a transaction that is not a business combination and that affect neither accounting nor taxable profit and temporary differences related to investments in subsidiaries where the Bank is able to control the timing of the reversal of the temporary difference and it is probable that they will not reverse in the foreseeable future.

Deferred tax assets are recognised for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be used. Future taxable profits are determined based on the reversal of relevant taxable temporary differences. If the amount of taxable temporary differences is insufficient to recognise a deferred tax asset in full, then future taxable profits, adjusted for reversals of existing temporary differences, are considered, based on the business plans for individual subsidiaries in the Bank. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised; such reductions are reversed when the probability of future taxable profits improves.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

The measurement of deferred taxes reflects the tax consequences that would follow the manner in which the Bank expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Interest and similar income and expense

Interest income and expense are recognised in profit or loss using the effective interest method.

(Thousands of Russian Roubles)

When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument, but does not consider future credit losses. The calculation includes all fees directly related to the loan issuance and amounts paid or received between the parties to the contract that are an integral part of the effective interest rate, including incremental directly attributable loan origination costs, such as bonuses for loan issuance. Once the balance value of a financial asset or group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the original effective interest rate applied to the new carrying amount.

Fee and commission income

The Bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into two categories described below:

Fee income earned from services that are provided over a certain period of time

Fees earned for the provision of services over a period of time are amortised over that period. These fees include commission income and asset management, custody and other management and advisory fees. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan.

Fee income from providing transaction services

Fees arising from negotiating or participating in the negotiation of a transaction for a third party – such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses – are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

Segment reporting

An operating segment is a component of the Bank that is engaged in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the Bank); whose operating results are regularly reviewed by the chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. Substantially all of the Bank's activities relate to provision of financial services mostly to corporate customers (small, medium and large business). Therefore, management concluded that the Bank has a single reportable segment.

New standards not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective as at 31 December 2017, and are not applied in preparing these consolidated financial statements. Of these pronouncements, potentially the following will have an impact on the financial position and performance. The Bank plans to adopt these pronouncements when they become effective.

IFRS 16 *Leases*

The standard is effective for annual periods beginning on or after 1 January 2019. Early adoption is permitted for entities that apply IFRS 15 *Revenue from Contracts with Customers* at or before the date of initial application of IFRS 16.

IFRS 16 replaces existing leases guidance including IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement contains a Lease*, SIC-15 *Operating Leases—Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. In addition, the nature of expenses related to those leases will now change as IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. There are recognition exemptions for short-term leases and leases of low value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases.

The Bank plans to apply IFRS 16 initially on 1 January 2019, using the modified retrospective approach with optional practical expedients. Therefore, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2019, with no restatement of comparative information.

The Bank has completed an initial assessment of the potential impact on its consolidated financial statements but has not yet completed its detailed assessment. The actual impact of applying IFRS 16 on the consolidated financial statements in the period of initial application will depend on future economic conditions, including the Bank's borrowing rates at 1 January 2019, the composition of the Bank's lease portfolio at that date, the Bank's latest assessment of whether it will exercise any lease renewal options and the extent to which the Bank chooses to use practical expedients and recognition exemptions.

So far, the most significant impact identified is that the Bank will recognise new assets and liabilities for its operating leases of office buildings. As at 31 December 2017, the Bank's future minimum lease payments under non-cancellable operating leases amounted to RUB 1 067 896 thousand, on an undiscounted basis (see Note 21).

(Thousands of Russian Roubles)

IFRS 15 *Revenue from Contracts with Customers*

The Bank is required to adopt IFRS 15 *Revenue from Contracts with Customers* from 1 January 2018.

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS *18 Revenue*, IAS 11 *Construction Contracts* and IFRIC 13 *Customer Loyalty Programmes*. IFRS 15 provides a single comprehensive model to use when accounting for revenue arising from contracts with customers. The new model applies to all contracts with customers except those that are within the scope of other IFRSs such as financial instruments, leases and insurance contracts. As a result, the majority of the Bank's revenue, including net interest income, will not be impacted.

The Bank plans to adopt IFRS 15 using the cumulative effect method, with the effect of initially applying this standard recognised at the date of initial application (i.e. 1 January 2018). As a result, the Bank will not apply the requirements of IFRS 15 to the comparative period presented.

The Bank is continuing to review its revenue contracts that fall within the scope of IFRS 15 and to assess the impact of the new standard on its consolidated financial statements, including the additional disclosure requirements. While the impact assessment is not complete, the Bank does not currently expect the adoption of IFRS 15 to have a significant impact on its consolidated financial statements.

IFRS 9 *Financial instruments*

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments*. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. It replaces IAS *39 Financial Instruments: Recognition and Measurement*.

In October 2017, the IASB issued *Prepayment Features with Negative Compensation (Amendments to IFRS 9)*. The amendments are effective for annual periods beginning on or after 1 January 2019, with early adoption permitted.

The Bank will apply IFRS 9 as issued in July 2014 initially on 1 January 2018 and will early adopt the amendments to IFRS 9 on the same date.

i. Classification – Financial assets

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics.

IFRS 9 includes three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). It eliminates the existing IAS 39 categories of held to maturity, loans and receivables and available for sale.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is to hold assets 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 (SPPI) on the principal amount outstanding.

A financial asset is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the Bank may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis.

All financial assets not classified as measured at amortised cost or FVOCI as described above are measured at FVTPL. In addition, on initial recognition the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

A financial asset is classified into one of these categories on initial recognition. See (vii) for the transition requirements relating to classification of financial assets.

Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of IFRS 9 are not separated. Instead, the hybrid financial instrument as a whole is assessed for classification.

(Thousands of Russian Roubles)

Business model assessment

The Bank will make an assessment of the objective of the business model in which a financial asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information that will be considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice, including whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading and those that are managed and whose performance is evaluated on a fair value basis will be measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessment whether contractual cash flows are solely payments of principal and interest

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest ("SPPI"), the Bank will consider the contractual terms of the instrument. This will include assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank will consider:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets – e.g. non-recourse asset arrangements; and
- features that modify consideration for the time value of money – e.g. periodic reset of interest rates.

All of the Bank's loans contain prepayment features.

A prepayment feature is consistent with the SPPI criterion if the prepayment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable compensation for early termination of the contract.

In addition, a prepayment feature is treated as consistent with this criterion if a financial asset is acquired or originated at a premium or discount to its contractual par amount, the prepayment amount substantially represents the contractual par amount plus accrued (but unpaid) contractual interest (which may also include reasonable compensation for early termination), and the fair value of the prepayment feature is insignificant on initial recognition.

Impact assessment

The Bank has finalised the business models assessment. The Bank is currently in the process of verification and testing of automated tool for registering SPPI assessment results.

The standard will affect the classification and measurement of financial assets held as at 1 January 2018 as follows.

- Derivative financial assets held for risk management, measured at FVTPL under IAS 39, will also be measured at FVTPL under IFRS 9.
- Amounts due from credit institutions and Loans to customers that are classified as loans and receivables and measured at amortised cost under IAS 39 will in general also be measured at amortised cost under IFRS 9.
- Debt investment securities that are classified as available-for-sale under IAS 39 may, under IFRS 9, be measured at amortised cost, FVOCI or FVTPL, depending on the particular circumstances.

The Bank has estimated that, on the adoption of IFRS 9 at 1 January 2018, the impact of applying the new classification and measurement requirements is not significant.

(Thousands of Russian Roubles)

ii. Impairment – Financial assets, loan commitments and financial guarantee contracts

IFRS 9 replaces the ‘incurred loss’ model in IAS 39 with a forward-looking ‘expected credit loss’ (ELC) model. This will require considerable judgement over how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis.

The new impairment model applies to the following financial instruments that are not measured at FVTPL:

- financial assets that are debt instruments;
- lease receivables; and
- loan commitments and financial guarantee contracts issued (previously, impairment was measured under IAS 37 Provisions, Contingent Liabilities and Contingent Assets).

Under IFRS 9, no impairment loss is recognised on equity investments.

IFRS 9 requires a loss allowance to be recognised at an amount equal to either 12-month ECLs or lifetime ECLs. Lifetime ECLs are the ECLs that result from all possible default events over the expected life of a financial instrument, whereas 12-month ECLs are the portion of ECLs that result from default events that are possible within the 12 months after the reporting date.

The Bank will recognise loss allowances at an amount equal to lifetime ECLs, except in the following cases, for which the amount recognised will be 12-month ECLs:

- debt investment securities and intragroup balances that are determined to have low credit risk at the reporting date; and
- other financial instruments for which credit risk has not increased significantly since initial recognition.

The impairment requirements of IFRS 9 are complex and require management judgements, estimates and assumptions, particularly in the following areas, which are discussed in detail below:

- assessing whether the credit risk of an instrument has increased significantly since initial recognition; and
- incorporating forward-looking information into the measurement of ECLs.

Measurement of ECLs

ECLs are a probability-weighted estimate of credit losses and will be measured as follows:

- *financial assets that are not credit-impaired at the reporting date*: the present value of all cash shortfalls – i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive;
- *financial assets that are credit-impaired at the reporting date*: the difference between the gross carrying amount and the present value of estimated future cash flows;
- *undrawn loan commitments*: the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive; and
- *financial guarantee contracts*: the present value of the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

Financial assets that are credit-impaired are defined by IFRS 9 in a similar way to financial assets that are impaired under IAS 39.

Definition of default

Under IFRS 9, the Bank will consider a financial asset to be in default when:

- *Doubtful:* the borrower is under the bankruptcy procedure or in the equivalent status regardless of the Bank’s estimated losses;
- *Unlikely to pay:* the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realising security (if any is held), for any other reason except for the bankruptcy or an equivalent; or
- *90 days past due:* the borrower is more than 90 days past due on any material credit obligation to the Bank.

In assessing whether a borrower is in default, the Bank will consider both qualitative and quantitave indicators based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Significant increase in credit risk

The Bank has established a framework that incorporates both quantitative and qualitative information to determine whether the credit risk on a particular financial instrument has increased significantly since initial recognition. The framework aligns with the Bank’s internal credit risk management process.

(Thousands of Russian Roubles)

In certain instances, using its expert credit judgement and, where possible, relevant historical experience, the Bank may determine that an exposure has undergone a significant increase in credit risk if particular qualitative factors indicate so and those indicators may not be fully captured by its quantitative analysis on a timely basis. As a backstop, and as required by IFRS 9, the Bank will presumptively consider that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. The Bank will determine days past due by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received.

Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value.

Under IFRS 9, when the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly is performed.

The Bank renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Bank's forbearance policy, loan forbearance is granted on a selective basis if the debtor may experience difficulties in servicing the debt, is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity and changing the timing of interest. Both retail and corporate loans are subject to the forbearance policy. Generally, forbearance is a qualitative indicator of significant increase in credit risk for performing loans. Following forbearance, a customer needs to demonstrate consistently good payment behaviour over a period of time before the loss allowance reverts to being measured at an amount equal to 12-month ECLs.

Inputs into measurement of ECLs

The key inputs into the measurement of ECLs are likely to be the term structures of the following variables:

- PD;
- loss given default (LGD); and
- exposure at default (EAD).

These parameters will be derived from internally developed statistical models and will be adjusted to reflect forward-looking information.

PD estimates are estimates at a certain date, which will be calculated based on statistical models. These statistical models will be based on internally compiled data comprising both quantitative and qualitative factors.

LGD is the magnitude of the likely loss if there is a default. The LGD models will consider the segment of the loan based on internal risk-management segmentation and the collateral coverage of the loan. LGD estimates will be calibrated for different economic scenarios. They will be calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Bank will derive the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract, including amortisation, and prepayments. The EAD of a financial asset will be the gross carrying amount at default. For lending commitments and financial guarantees, the EAD will consider the amount drawn, as well as potential future amounts that may be drawn or repaid under the contract.

Where modelling of a parameter is carried out on a collective basis, the financial instruments will be grouped on the basis of shared risk characteristics that include:

- instrument type;
- annual turnover (revenue);
- collateral type for retail loans;
- collateral coverage.

The groupings will be subject to regular review to ensure that exposures within a particular group remain appropriately homogeneous.

For portfolios in respect of which the Bank has limited historical data, external benchmark information will be used to supplement the internally available data.

Impact assessment

The most significant impact on the Bank's financial statements from the implementation of IFRS 9 is expected to result from the new impairment requirements. Impairment losses will increase and become more volatile for financial instruments in the scope of the IFRS 9 impairment model. Currently the Bank is in process of refining and finalising its models of ECL calculations and is in process assessing the impact of the new impairment requirements.

(Thousands of Russian Roubles)

iii. Classification – Financial liabilities

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

iv. Derecognition and contract modification

IFRS 9 incorporates the requirements of IAS 39 for the derecognition of financial assets and financial liabilities without substantive amendments.

However, it contains specific guidance for the accounting when the modification of a financial instrument not measured at FVTPL does not result in derecognition. Under IFRS 9, the Bank will recalculate the gross carrying amount of the financial asset (or the amortised cost of the financial liability) by discounting the modified contractual cash flows at the original effective interest rate and recognise any resulting adjustment as a modification gain or loss in profit or loss. Under IAS 39, the Bank does not recognise any gain or loss in profit or loss on modifications of financial liabilities and non-distressed financial assets that do not lead to their derecognition.

v. Disclosures

IFRS 9 will require extensive new disclosures, in particular about credit risk and ECLs.

vi. Impact on capital planning

Currently the Bank assesses that the adoption of IFRS 9 will not have impact on statutory capital of the Bank (Note 28); however, further developments in the regulatory environment in respect of this aspect may take place in the near future.

vii. Transition

Changes in accounting policies resulting from the adoption of IFRS 9 will generally be applied retrospectively, except as described below.

The Bank will take advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 will generally be recognised in retained earnings and reserves as at 1 January 2018.

The following assessments have to be made on the basis of the facts and circumstances that exist at the date of initial application.

- The determination of the business model within which a financial asset is held.
- The designation and revocation of previous designations of certain financial assets and financial liabilities as measured at FVTPL.
- The designation of certain investments in equity instruments not held for trading as at FVOCI.

If a debt investment security has low credit risk at 1 January 2018, then the Bank will determine that the credit risk on the asset has not increased significantly since initial recognition.

Other standards

The following amended standards and interpretations are not expected to have a significant impact on the Group's consolidated financial statements.

— *Annual Improvements to IFRSs 2014-2016 Cycle – Amendments to IFRS 1 and IAS 28.*

— *Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2).*

— *Transfers of Investment Property (Amendments to IAS 40).*

— *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28).*

— *IFRIC 22 Foreign Currency Transactions and Advance Consideration.*

— *IFRIC 23 Uncertainty over Income Tax Treatments.*

— *IFRS 17 Insurance Contracts*

(Thousands of Russian Roubles)

4. Cash and cash equivalents

Cash and cash equivalents as at 31 December comprise:

	2017	*2016*
Cash on hand	742 319	847 901
Correspondent accounts with the CBR	1 988 527	1 156 597
Correspondent accounts and overnight placements with other credit institutions		
- OECD banks	1 139 061	1 889 134
- Other foreign banks	9 353	360
- Largest 30 Russian banks	111	8 837
- Other Russian banks	6 924	15 404
Cash and cash equivalents	**3 886 295**	**3 918 233**

As at 31 December 2017, the Bank has one bank (2016: no banks), whose balances exceed 10% of equity. The gross value of these balances as at 31 December 2017 is RUB 1 988 527 thousand.

Amounts of cash and cash equivalents include balances with related parties, which are disclosed in Note 27. The gross value of these balances as at 31 December 2017 is RUB 1 048 146 thousand (2016: RUB 1 813 912 thousand). They bear annual interest rate -0.50% for EUR, 0.07% for USD and -0.75% for other currencies (2016: -0.50% for EUR, 0.07% for USD, -0.75% for other currencies).

No cash and cash equivalents are impaired or past due.

5. Amounts due from credit institutions

Amounts due from credit institutions as at 31 December comprise:

	2017	*2016*
Time deposit with the CBR	7 005 938	5 502 781
Time deposits with credit institutions		
- OECD banks	2 728 577	2 426 387
- Largest 30 Russian banks	1 700 671	2 206 295
- Other Russian banks	-	1 152 297
- Other banks	2 101 155	958 792
Gross amounts due from credit institutions	**13 536 341**	**12 246 552**
Less: Impairment allowance	(7 604)	(8 634)
Net amounts due from credit institutions	**13 528 737**	**12 237 918**

Movements in the impairment allowance for the year ended 31 December are as follows:

	2017	*2016*
Impairment allowance as at 1 January	**8 634**	**15 031**
Net recovery	(1 030)	(6 397)
Impairment allowance as at 31 December	**7 604**	**8 634**

As at 31 December 2017, the Bank has three banks (2016: two banks), whose balances individually exceed 10% of equity. The gross value of these balances as at 31 December 2017 is RUB 11 135 397 thousand (2016: RUB 7 929 168 thousand).

Amounts due from credit institutions include loans placed with related parties, which are disclosed in Note 27. The gross value of these balances as at 31 December 2017 is RUB 2 728 577 thousand (2016: RUB 2 426 747 thousand). They bear annual interest rates 1.58% for USD and 7.65% for RUB (2016: 1.65% for USD and 0.00% for CNY).

(Thousands of Russian Roubles)

6. Available-for-sale securities

Available-for-sale securities as at 31 December comprise:

	2017	*2016*
Russian State bonds ("OFZ")	3 625 584	3 535 812
The CBR bonds ("KOBR")	505 315	-
Available-for-sale securities	**4 130 899**	**3 535 812**

As at 31 December 2017 and 2016, Russian State bonds are RUB denominated securities issued by the Ministry of Finance of the Russian Federation. Russian State bonds have maturity dates from 31 January 2018 to 29 January 2020 (2016: from 19 April 2017 to 16 October 2019), annual coupon rates from 6.2% to 10.4% (2016: from 6.2% to 11.0%) and annual yields to maturity from 5.8% to 8.3% (2016: from 8.3% to 10.2%), depending on the bond issue.

As at 31 December 2017, the CBR bonds are RUB denominated securities with the maturity date on 14 February 2018, annual coupon rate of 7.75 % and annual yield to maturity of 7.92 %.

As at 31 December 2017 and 2016, there are no available-for-sale securities which are impaired or past due.
As at 31 December 2017 and 2016, the Bank has no transactions to sell securities under agreements to purchase.

As at 31 December 2017, available-for-sale securities totalling RUB 2 078 544 thousand are eligible for pledge within the limits of refinancing from the CBR (2016: RUB 2 039 797 thousand).

7. Derivative financial instruments

The Bank enters into derivative financial instruments for trading purposes. The notional amount, recorded gross, is the amount of a derivative's underlying asset, and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk.

The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts as at 31 December:

	2017			*2016*		
	Notional amount	*Fair values Asset*	*Fair values Liability*	*Notional amount*	*Fair values Asset*	*Fair values Liability*
Foreign exchange contracts						
Spot deals – foreign counterparties	-	-	-	600 000	-	(664)
Spot deals – domestic counterparties	-	-	-	-	-	-
Swap deals – domestic counterparties	-	-	-	2 588 716	1 735	(122)
Forwards – domestic counterparties	-	-	-	-	-	-
Total derivative financial assets (liabilities)	**-**	**-**	**-**	**-**	**1 735**	**(786)**

(Thousands of Russian Roubles)

8. Loans to customers

Loans to customers as at 31 December comprise:

	2017	*2016*
Loans to large corporate customers		
Large corporate loans	15 520 323	17 426 557
Gross loans to large corporate customers	**15 520 323**	**17 426 557**
Less: Loan impairment allowance	(2 569 361)	(4 056 351)
Net loans to large corporate customers	**12 950 962**	**13 370 206**
Small and medium corporate customers		
Medium loans	9 304 816	8 741 544
Small loans	5 432 513	6 790 482
Micro loans	851 825	1 736 535
Overdrafts	496 748	542 700
Gross loans to small and medium corporate customers	**16 085 902**	**17 811 261**
Less: Loan impairment allowance	(1 803 231)	(2 241 792)
Net loans to small and medium corporate customers	**14 282 671**	**15 569 469**
Loans to retail customers		
Consumer loans	1 110 963	873 621
Mortgage loans	691 313	762 096
Credit cards	105 072	110 760
Gross loans to retail customers	**1 907 348**	**1 746 477**
Less: Loan impairment allowance	(145 893)	(148 501)
Net loans to retail customers	**1 761 455**	**1 597 976**
Total gross loans to customers	**33 513 573**	**36 984 295**
Less: Loan impairment allowance	(4 518 485)	(6 446 644)
Total net loans to customers	**28 995 088**	**30 537 651**

Movements in the loan impairment allowance for the year ended 31 December 2017 is as follows:

	Loans to large corporate customers	***Loans to small and medium corporate customers***	***Loans to retail customers***	***Total loans to customers***
Loan impairment allowance as at 1 January	**4 056 351**	**2 241 792**	**148 501**	**6 446 644**
Net (recovery) charge	(64 961)	367 027	14 762	316 828
Effect of unwinding of discount	(7 816)	(251 139)	(9 293)	(268 248)
Amounts written off / sold	(1 414 213)	(554 449)	(8 077)	(1 976 739)
Loan impairment allowance as at 31 December	**2 569 361**	**1 803 231**	**145 893**	**4 518 485**

Movements in the loan impairment allowance for the year ended 31 December 2016 is as follows:

	Loans to large corporate customers	***Loans to small and medium corporate customers***	***Loans to retail customers***	***Total loans to customers***
Loan impairment allowance as at 1 January	**4 144 352**	**2 867 794**	**425 466**	**7 437 612**
Net charge	570 099	332 375	39 656	942 130
Effect of unwinding of discount	(6 388)	(248 004)	(10 225)	(264 617)
Amounts written off / sold	(651 712)	(710 373)	(306 396)	(1 668 481)
Loan impairment allowance as at 31 December	**4 056 351**	**2 241 792**	**148 501**	**6 446 644**

As at 31 December 2017, the total gross amount of overdue outstanding payments on loans less accrued interest is RUB 4 921 792 thousand (2016: RUB 6 289 533 thousand). Interest income on impaired loans for 2017 equals to RUB 610 305 thousand (2016: RUB 662 514 thousand).

Amounts of loans to customers include balances with related parties, which are disclosed in Note 27.

(Thousands of Russian Roubles)

Concentration of loans to customers

Economic sector risk concentrations within loans to customers are as follows:

	2017		2016	
	Amount	*%*	*Amount*	*%*
Trading	12 636 730	38	15 331 146	41
Services	9 365 348	28	9 297 209	25
Manufacturing	8 423 183	25	9 111 632	25
Individuals	1 907 348	6	1 746 477	5
Other	1 180 964	3	1 497 831	4
Total gross loans to customers	**33 513 573**	**100**	**36 984 295**	**100**

As at 31 December 2017, the Bank has twenty largest borrowers with an aggregate loan amount for each of them above RUB 200 180 thousand (2016: twenty largest borrowers above RUB 234 650 thousand). The total aggregate amount of these loans is RUB 11 864 970 thousand or 35.4% of the gross loan portfolio (2016: RUB 9 848 728 thousand or 26.6%), with the impairment allowance of RUB 1 659 182 thousand (2016: RUB 2 387 273 thousand).

9. Net investments in finance leases

Net investments in finance leases at 31 December 2017 comprise:

	Within 1 year	*From 1 to 5 years*	*Total*
Gross investments in finance leases	865 859	829 129	**1 694 988**
Unearned future finance income on finance leases	(77 906)	(188 369)	**(266 275)**
	787 953	**640 760**	**1 428 713**
Less: Impairment allowance	(45 331)	(49 265)	**(94 596)**
Net investments in finance leases	**742 622**	**591 495**	**1 334 117**

Net investments in finance leases at 31 December 2016 comprise:

	Within 1 year	*From 1 to 5 years*	*Total*
Gross investments in finance leases	833 680	472 629	**1 306 309**
Unearned future finance income on finance leases	(76 393)	(133 676)	**(210 069)**
	757 287	**338 953**	**1 096 240**
Less: Impairment allowance	(61 021)	(37 042)	**(98 063)**
Net investments in finance leases	**696 266**	**301 911**	**998 177**

Movements in the allowance for impairment of investments in finance leases for the year ended 31 December are as follows:

	2017	*2016*
Impairment allowance as at 1 January	**98 063**	**252 999**
Net charge	4 154	18 012
Effect of unwinding of discount	(5 494)	(4 526)
Amounts written off / sold	(2 127)	(168 422)
Impairment allowance as at 31 December	**94 596**	**98 063**

The leased assets are effectively pledged, as the rights to the leased asset revert to the lessor in the event of default. Lease payments are due on a monthly basis. The Bank holds title to the leased property during the lease term. Risks related to the leased property such as damage caused by various reasons, theft and other are generally insured under finance lease agreements.

As at 31 December 2017, the Bank has twenty largest lessees with an aggregate gross amount for each of them above RUB 11 435 thousand (2016: twenty largest lessees above RUB 10 988 thousand). The total aggregate amount of gross investments in finance leases related to these leases is RUB 465 057 thousand or 32.6% of the total gross investments in finance leases portfolio (2016: RUB 382 662 thousand or 34.9%), with the impairment allowance of RUB 15 687 thousand (2016: RUB 34 606 thousand).

There is no unguaranteed residual value related to lease contracts outstanding as at 31 December 2017 and 2016.

(Thousands of Russian Roubles)

10. Impairment of loans, net investments in finance leases and amounts due from credit institutions

	2017	2016
Loans to large corporate customers	(64 961)	570 099
Loans to small and medium corporate customers	367 027	332 375
Loans to retail customers	14 762	39 656
Net investments in finance leases	4 154	18 012
Amounts due from credit institutions	(1 030)	(6 397)
Total impairment allowance	**319 952**	**953 745**

11. Property and equipment

The movements in property and equipment for the year ended 31 December are as follows:

	Premises and capital improve-ments	*Office and computer equipment*	*Total*
Cost as at 1 January 2016	451 572	957 468	1 409 040
Accumulated depreciation as at 1 January 2016	(157 089)	(838 683)	(995 772)
Carrying amount as at 1 January 2016	**294 483**	**118 785**	**413 268**
Additions	559	403 032	403 591
Disposals (net of accumulated depreciation)	(5 623)	(1 633)	(7 256)
Depreciation charge for the year	(15 014)	(97 946)	(112 960)
Cost as at 31 December 2016	446 281	1 254 116	1 700 397
Accumulated depreciation as at 31 December 2016	(171 876)	(831 878)	(1 003 754)
Carrying amount as at 31 December 2016	**274 405**	**422 238**	**696 643**
Additions	1 458	195 264	196 722
Disposals (net of accumulated depreciation)	(6 938)	(78 210)	(85 148)
Depreciation charge for the year	(15 367)	(141 813)	(157 180)
Revaluation of premises	480 180	-	480 180
Cost as at 31 December 2017	735 704	1 151 816	1 887 520
Accumulated depreciation as at 31 December 2017	(1 966)	(754 337)	(756 303)
Carrying amount at 31 December 2017	**733 738**	**397 479**	**1 131 217**

Additions for the year 2016 include computer facilities in the amount of RUB 391 077 thousand, acquired for the purpose of organisation of Data Processing Centre located in Moscow and Saint-Petersburg (“DPC”). Creation of DPC is stipulated by adoption of Federal Law No. 242-FZ dated 21 July 2014 *On Amendments to Certain Legislative Acts of the Russian Federation to Clarify the Procedure of Personal Data Processing in Information and Telecommunication Networks*, resulted in storage of personal information on the territory of the Russian Federation.

Capital expenditure commitments related to property and equipment are disclosed in Note 21.

As at 1 January 2018, premises were revalued by the Bank’s management based on the results of an appraisal performed by a professional appraiser firm that possesses recognised qualifications and has relevant experience in performing valuation of premises. The income capitalisation approach was used for the revaluation of premises. As a result of revaluation the carrying value increased by RUB 480 180 thousand, of which RUB 384 144 thousand (net of income tax) was recognised in other comprehensive income.

The income capitalisation method consists in an analysis of income and expenses related to the appraised building, and in the measurement of its fair value by their capitalisation.

The following key assumptions are used in applying the income capitalisation approach:

- the calculation of annual income is based on estimated rental income net of maintenance and technical service expenses related to the buildings, calculated based on current market rental rates and average maintenance and technical service costs;

- a capitalisation rates of 9.5% and 11% are used for capitalisation of net annual income;

- losses from underutilisation were estimated as not significant.

(Thousands of Russian Roubles)

Changes in the estimates above could affect the value of the premises.To the extent that the net present value of the estimated cash flows used in the income capitalisation approach differs by plus/minus ten percent, the premises valuation as at 31 December 2017 would be RUB 51 863 thousand lower/higher.

The fair values of the Bank's premises are categorised into Level 3 of the fair value hierarchy.

The carrying value of premises as at 31 December 2017, if the premises had not been revalued, would be RUB 253 558 thousand.

12. Intangible assets

The movements in intangible assets for the year ended 31 December are as follows:

	Computer software and licenses
Cost as at 1 January 2016	2 845 406
Accumulated amortisation as at 1 January 2016	(2 300 869)
Carrying amount as at 1 January 2016	**544 537**
Additions	446 951
Disposals (net of accumulated amortisation)	(1 169)
Amortisation for the year	(269 747)
Cost as at 31 December 2016	2 517 811
Accumulated amortisation as at 31 December 2016	(1 797 239)
Carrying amount as at 31 December 2016	**720 572**
Additions	154 446
Disposals (net of accumulated amortisation)	(7 074)
Amortisation for the year	(282 277)
Cost as at 31 December 2017	2 114 463
Accumulated amortisation as at 31 December 2017	(1 528 796)
Carrying amount as at 31 December 2017	**585 667**

Additions for the year 2016 also include intangible assets (computer software and licenses) in the amount of RUB 356 411 thousand acquired for the purpose of organisation of the DPC.

Capital expenditure commitments related to intangible assets are disclosed in Note 21.

13. Taxation

The corporate income tax expense for the year ended 31 December comprises:

	2017	***2016***
Current tax	73 404	41 285
Deferred tax – origination and reversal of temporary differences	202 104	52 154
Total income tax expense	**275 508**	**93 439**

The Bank is liable for current income tax in Russia on its taxable profit and capital gains other than profits on certain types of securities at a rate of 20% (2016: 20%). Pursuant to Russian income tax law interest income on certain types of securities is subject to income tax at a rate of 15%, 9% or nil. As at 31 December 2017, the rate of tax applicable for deferred taxes is 20% (2016: 20%).

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual for the year ended 31 December is as follows:

	2017	***2016***
Profit before income tax	**277 579**	**450 899**
Income tax expense at the applicable tax rate	55 516	90 180
Income on government securities taxed at different rates	(16 393)	(13 762)
Underprovided in prior periods	66 798	-
Non-deductible expenses	169 587	17 021
Total income tax expense	**275 508**	**93 439**
Effective tax rate	**96.6%**	**20.7%**

(Thousands of Russian Roubles)

Temporary differences between the carrying amounts of assets for financial reporting purposes and the amounts used for taxation purposes give rise to net deferred tax assets as at 31 December 2017 and 2016.

The deductible temporary differences do not expire under the current tax legislation.

As at 31 December 2017, the Bank Intesa (Joint-Stock Company) has the tax loss carry-forwards of RUB 513 386 thousand (2016: RUB 461 648 thousand). Based on the analysis of the business plan and the future cash flows, the Bank assumes that the deferred tax asset will be fully utilised.

Bank Intesa (Joint-Stock Company) and AO "Intesa Leasing" calculate net deferred tax assets and liabilities separately and cannot offset them.

As at 31 December 2017, AO "Intesa Leasing" has no tax loss carry-forwards (2016: RUB 10 817 thousand).

Movement in temporary differences during the year ended 31 December 2017 are as follows:

	1 January 2017	*Recognised in profit or loss*	*Recognised in other comprehensive income*	*31 December 2017*
Tax effect of temporary differences				
Available-for-sale securities	(5 457)	-	(244)	(5 701)
Derivative financial instruments	(190)	-	-	(190)
Loans to customers	(142 431)	(147 563)	-	(289 994)
Net investments in finance leases	79 610	(18 218)	-	61 392
Property, equipment and intangible assets	(32 298)	4 104	(96 036)	(124 230)
Other assets	163 893	(90 853)	-	73 040
Other liabilities	91 140	9 505	-	100 645
Tax loss carry-forwards	472 465	40 921	-	513 386
Net deferred tax assets	**626 732**	**(202 104)**	**(96 280)**	**328 348**

Movement in temporary differences during the year ended 31 December 2016 are as follows:

	1 January 2016	*Recognised in profit or loss*	*Recognised in other comprehensive income*	*31 December 2016*
Tax effect of temporary differences				
Available-for-sale securities	(2 494)	-	(2 963)	(5 457)
Derivative financial instruments	8 377	(8 567)	-	(190)
Loans to customers	(49 608)	(92 823)	-	(142 431)
Net investments in finance leases	126 387	(46 777)	-	79 610
Property, equipment and intangible assets	1 375	(33 673)	-	(32 298)
Other assets	135 275	28 618	-	163 893
Other liabilities	50 673	40 467	-	91 140
Tax loss carry-forwards	411 864	60 601	-	472 465
Net deferred tax assets	**681 849**	**(52 154)**	**(2 963)**	**626 732**

14. Other impairment and provisions

Movements in the other impairment allowances and provisions for the year ended 31 December are as follows:

	Other assets	*Credit related commitments*	*Provisions for other claims*	*Total*
1 January 2016	**259 463**	**163 042**	**34 680**	**457 185**
Net charge (recovery)	18 060	40 889	(13 428)	45 521
Amounts written off	(222 810)	-	-	(222 810)
31 December 2016	**54 713**	**203 931**	**21 252**	**279 896**
Net charge	49 039	43 390	16 418	108 847
Amounts written off	(47 629)	-	-	(47 629)
31 December 2017	**56 123**	**247 321**	**37 670**	**341 114**

(Thousands of Russian Roubles)

Impairment allowances for assets are deducted from the carrying amounts of the related assets. Provisions for claims, guarantees and commitments are recorded in other liabilities.

15. Other assets and liabilities

Other assets as at 31 December comprise:

	2017	*2016*
Amounts held in clearing organisations	125 455	52 991
Settlements with suppliers and customers	105 359	649 815
Other financial assets	**230 814**	**702 806**
Prepayments	294 227	388 592
Repossessed collateral	194 854	207 738
Construction in progress	63 043	32 886
Current income tax assets and other tax assets	52 296	11 375
Leasehold improvements	50 386	68 164
Other	44 906	28 255
Other non-financial assets before impairment allowance	**699 712**	**737 010**
Less: Impairment allowance	(56 123)	(54 713)
Other non-financial assets	**643 589**	**682 297**
Other assets	**874 403**	**1 385 103**

Other liabilities as at 31 December comprise:

	2017	*2016*
Settlements with suppliers and customers	224 171	283 946
Other financial liabilities	**224 171**	**283 946**
Provision for losses on credit related commitments	247 321	203 931
Settlements with employees	97 187	107 933
Provision for other claims	37 670	21 252
Tax liabilities other than income tax	25 194	43 025
Other	114 969	81 416
Other non-financial liabilities	**522 341**	**457 557**
Other liabilities	**746 512**	**741 503**

16. Amounts due to credit institutions

Amounts due to credit institutions as at 31 December comprise:

	2017	*2016*
Time deposits and loans	4 914 148	4 764 784
Correspondent accounts	970 502	2 095 961
Amounts due to credit institutions	**5 884 650**	**6 860 745**

As at 31 December 2017, the Bank has two banks (2016: three banks), whose balances individually exceed 10% of equity. The gross value of these balances as at 31 December 2017 is RUB 3 033 445 thousand (2016: RUB 6 848 360 thousand).

Amounts due to credit institutions include loans from related parties, which are disclosed in Note 27. The gross value of these balances as at 31 December 2017 is RUB 964 454 thousand (2016: RUB 3 364 525 thousand), 0.00% annual interest rate (2016: 0.00% annual interest rate).

At 31 December 2017, the Bank attracted funds from credit institutions to issue loans to customers in the amount of RUB 1 532 849 thousand (2016: RUB 1 874 545 thousand).

(Thousands of Russian Roubles)

17. Amounts due to customers

The amounts due to customers as at 31 December include the following:

	2017	*2016*
Legal entities	**13 616 591**	**18 438 518**
- current accounts	10 318 112	10 114 911
- term deposits	3 298 479	8 323 607
Individuals	**16 826 402**	**9 477 458**
- current accounts	1 931 215	1 670 600
- term deposits	14 895 187	7 806 858
State and non-profit organisations	**84 112**	**49 095**
- current accounts	47 268	39 958
- term deposits	36 844	9 137
Amounts due to customers	**30 527 105**	**27 965 071**

State and non-profit organisations exclude government-owned profit oriented organisations. Amounts received from individual enterpreneurs are classified as amounts due to legal entities.

As at 31 December 2017, the Bank has one customer (2016: one customer), whose balances individually exceed 10% of equity. The gross value of this balance as at 31 December 2017 is RUB 5 487 264 thousand or 17.98% of total amounts due to customers (2016: RUB 5 220 635 thousand, 18.67% of total amounts due to customers).

As at 31 December 2017, included in term deposits are deposits of individuals of RUB 14 895 187 thousand (2016: RUB 7 806 858 thousand). In accordance with the Russian Civil Code, the Bank is obliged to repay such deposits upon demand of a depositor. In case a term deposit is repaid upon demand of the depositor prior to maturity, interest on it is paid based on the interest rate for demand deposits, unless a different interest rate is specified in the agreement.

18. Debt securities issued

In June 2017 the Bank repaid part of the RUB 5 000 000 thousand bond issue in the nominal amount of RUB 1 686 508 thousand.

As at 31 December 2017, the Bank has non-convertible documentary bonds in nominal amount totaling RUB 130 643 thousand, with a contractual maturity in June 2018, with a current annual coupon rate 8.25% payable semi-annually (as at 31 December 2016: RUB 1 817 151 thousand, with a contractual maturity in June 2018 with a current annual coupon rate 10.55% payable semi-annually), and non-convertible documentary bonds in nominal amount totaling RUB 3 000 000 thousand with a contractual maturity in October 2019, with an annual coupon rate 9.75% payable semi-annually (as at 31 December 2016: RUB 3 000 000 thousand with a contractual maturity in October 2019, with an annual coupon rate 9.75% payable semi-annually).

19. Subordinated debt

As at 31 December 2017 and 31 December 2016, subordinated debt is represented by the loan from Intesa Sanpaolo Bank Luxembourg. This subordinated loan is denominated in US dollars and matures in December 2022. The annual interest rate on this subordinated loan is fixed, at the level of 6.58%.

The claims of the Bank’s creditors on subordinated debt shall only be satisfied after all claims of other creditors of the Bank are satisfied in full.

(Thousands of Russian Roubles)

Reconciliation of movements of liabilities to cash flows arising from financing activities

	Liabilities		
	Debt securities issued	**Subordinated debt**	**Total**
Balance as at 1 January 2016	5 028 641	2 915 308	**7 943 949**
Changes from financing cash flows			
Debt securities issued	3 350 000	-	3 350 000
Repayment of debt securities issued	(3 532 849)	-	(3 532 849)
Total changes from financing cash flows	**(182 849)**	**-**	**(1 686 508)**
The effect of changes in foreign exchange rates	**-**	**(488 596)**	**(488 596)**
Other changes	**29 314**	**-**	**29 314**
Balance at 31 December 2016	**4 875 106**	**2 426 712**	**7 301 818**
Balance as at 1 January 2017	4 875 106	2 426 712	**7 301 818**
Changes from financing cash flows			
Repayment of debt securities issued	(1 686 508)	-	(1 686 508)
Total changes from financing cash flows	**(1 686 508)**	**-**	**(1 686 508)**
The effect of changes in foreign exchange rates	**-**	**(121 873)**	**(121 873)**
Other changes	**(2 532)**	**-**	**(2 532)**
Balance at 31 December 2017	**3 186 066**	**2 304 839**	**5 490 905**

20. Equity

There were no movements in share capital for the years ended 31 December 2017 and 2016.

As at 31 December 2017 and 2016, the share capital of Banca Intesa (Joint-Stock Company) is represented by 876 128 ordinary shares with a nominal value of 12 350 RUB per share.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at annual and general meetings of the Bank.

Other capital reserve

As at 31 December 2017 and 2016, other capital reserve of RUB 1 803 914 thousand is represented by funds provided in June 2009 to the Bank by its shareholder Intesa Sanpaolo Holding International SA in the form of debt free financing. These funds are not repayable to the Bank's shareholder.

Revaluation reserve for available-for-sale securities

Revaluation reserve for available-for-sale securities records fair value changes on available-for-sale securities.

Revaluation of buildings

Revaluation reserve for buildings represents the result of change in model for the Bank's premises revaluation.

Retained earnings

In accordance with RAL, the Bank distributes profit as dividends or transfers it to retained earnings on the basis of accounting reports prepared in accordance with RAL. The Bank's accumulated loss under RAL as at 31 December 2017 is RUB 562 347 thousand (2016: accumulated loss RUB 282 573 thousand).

During 2017 and 2016, the Bank did not pay dividends in respect of the years ended 31 December 2016 and 31 December 2015.

21. Commitments and contingencies

Legal

In the ordinary course of business, the Bank is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Bank.

(Thousands of Russian Roubles)

Taxation

The taxation system in the Russian Federation continues to evolve and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are sometimes contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities who have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation.

Starting from 1 January 2012 new transfer pricing rules came into force in Russia. They provide the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of controllable transactions if their prices deviate from the market range or profitability range. According to the provisions of transfer pricing rules, the taxpayer should sequentially apply 5 methods of market price determination prescribed by the Tax Code.

Tax liabilities arising from transactions between companies are determined using actual transaction prices. It is possible with the evolution of the interpretation of the transfer pricing rules in the Russian Federation and the changes in the approach of the Russian tax authorities, that such transfer prices could be challenged. Given the short period since the current Russian transfer pricing rules became effective, the impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial position and/or the overall operations of the Bank.

In addition, starting from 1 January 2015 changes aimed at regulating tax consequences of transactions with foreign companies and their activities were introduced, such as concept of beneficial ownership of income, taxation of controlled foreign companies, tax residency rules, etc. These changes may potentially impact the Bank's tax position. This legislation and practice of its application is still evolving and the impact of legislative changes should be considered based on the actual circumstances.

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on the financial position, if the authorities were successful in enforcing their interpretations, could be significant.

The accumulated tax loss carry-forwards not utilized in the current year can be transferred for the future years without time limitation. Starting from 1 January 2017 till 31 December 2020 the income tax base can't be decreased by utilisation of tax loss carry-forwards for more than 50%.

Commitments

As at 31 December the Bank's commitments and contingencies comprise the following:

	2017	*2016*
Credit related commitments		
Guarantees issued	11 603 331	11 272 955
Undrawn credit line commitments	4 644 890	753 082
Undrawn overdraft loan commitments	988 473	1 350 262
Letters of credit	437 542	881 160
Commitments to issue loans	-	6 430
	17 674 236	**14 263 889**
Operating lease commitments		
Not later than 1 year	339 728	385 994
Later than 1 year but not later than 5 years	678 632	876 748
Later than 5 years	49 536	103 511
	1 067 896	**1 366 253**
Capital expenditure commitments – property and equipment	79	1 141
Capital expenditure commitments – intangible assets	76 975	127 823
	77 054	**128 964**
Less: Impairment allowance	(247 321)	(203 931)
Commitments and contingencies	**18 571 865**	**15 555 175**

The primary purpose of credit related commitments is to ensure that funds are available to a customer as required. Guarantees and 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, carry the same credit risk as loans.

(Thousands of Russian Roubles)

22. Net fee and commission income

Net fee and commission income for the year ended 31 December comprises:

	2017	*2016*
Fee and commission income		
Settlement transactions	422 949	432 501
Guarantees issued and letters of credit	201 236	262 060
Commission on consulting	101 835	547 123
Cash commissions	88 295	114 142
Accounts remote administration	70 552	81 629
Lending transactions	51 684	74 597
Other	79 103	69 958
Fee and commission income	**1 015 654**	**1 582 010**
Fee and commission expense		
Settlement transactions	76 446	82 593
Services on issuance and maintenance of plastic cards	26 638	17 326
Stock exchange services	18 658	6 476
Commission on consulting	6 292	-
Cash collection transactions	5 591	11 601
Commission on banknote transactions	4 284	4 711
Agency fee	2 890	1 809
Guarantees received	1 925	35 646
Other	2 554	884
Fee and commission expense	**145 278**	**161 046**
Net fee and commission income	**870 376**	**1 420 964**

Included in commission on lending transactions are fees and commissions charged during the life of the loan, for example, commission for amendments to the original terms and conditions of the loan agreement, commission for loan repayment prior to maturity and commission for information letters to the borrower.

Commission on consulting income represents investment and deal advisory commission received by the Bank.

23. Net losses from other operating activities

	2017	*2016*
Obligatory deposit insurance system contributions	(73 188)	(61 577)
Capital expenditures	(15 241)	(12 415)
Notarial and state duties expenses	(9 838)	(13 139)
Expenses for professional services	-	(141)
Net other operating income (losses)	29 560	(8 978)
Net losses from other operating activities	**(68 707)**	**(96 250)**

(Thousands of Russian Roubles)

24. Personnel and other general administrative expenses

Personnel expenses and other general administrative expenses for the year ended 31 December comprise:

	2017	*2016*
Salaries and bonuses	1 380 748	1 469 612
Social security costs	329 074	358 755
Personnel expenses	**1 709 822**	**1 828 367**
Operating lease	398 600	426 854
Data processing	279 568	380 385
Legal and consultancy expenses	262 520	274 312
Office materials	74 178	106 559
Communications	61 910	78 769
Security	37 585	47 608
Repair and maintenance of property and equipment	26 269	27 221
Marketing and advertising	24 349	16 583
Charity	19 805	23 765
Operating taxes	18 398	16 223
Insurance	15 311	21 321
Business and travel related expenses	13 816	15 962
Personnel training	940	774
Other	33 955	40 613
Other general administrative expenses	**1 267 204**	**1 476 949**

25. Corporate governance and risk management

Corporate governance framework

The Bank is established as a joint stock company in accordance with the Russian law. The supreme governing body of the Bank is the general shareholders meeting that convense for annual or extraordinary meetings. The general shareholders meeting makes strategic decisions on the Bank's operations.

The general shareholders meeting elects the Board of Directors. The Board of Directors is responsible for overall governance of the Bank's activities.

Russian legislation and the Charter of the Bank establish the lists of decisions that are exclusively approved by the general shareholders meeting and that are approved by the Board of Directors.

As at 31 December 2017, the Board of Directors includes:

- Professor Antonio Fallico – Chairman of the Board of Directors;
- Mr. Walter Ambrogi;
- Mr. Salvatore Catalano;
- Mr. Armando Selva;
- Mr. Luca Leoncini Bartoli;
- Mr. Christophe Velle;
- Mr. Giulio Ponti;
- Mr. Andrea Mascetti;
- Mr. Luca Santo Finazzi.

During the year ended 31 December 2017 one member left the Board of Directors, one new member joined it. No other changes occured in the composition of the Board of directors.

General activities of the Bank are managed by the sole executive body of the Bank - the Chairman of the Management Board and the collective executive body – the Management Board of the Bank. The Board of Directors meeting elects the Chairman of the Management Board. The executive bodies of the Bank are responsible for implementation of decisions of the general meeting of shareholders and the Board of Directors of the Bank. Executive bodies of the Bank report to the Board of Directors of the Bank and to the general meeting of shareholders.

As at 31 December 2017, the Management Board includes:

- Mr. Gianluca Corrias – Chairman of the Management Board;

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- Mrs. Olga Lein;
- Mrs. Tatyana Pavlycheva;
- Mrs. Irina Vasina;
- Mr. Oleg Dzhus;
- Mrs. Elena Grimaylo.

During 2017 one member left the Management Board. No other changes occured in the composition of the Management Board.

Internal control policies and procedures

Internal Control System ("ICS") consists of the set of rules, functions, organisational units, resources, processes and procedures aimed at ensuring that the following activities are performed, in accordance with the principles of sound and prudent management.

The purpose of internal controls is to ensure:

- effectiveness and efficiency of operations, effectiveness of asset and liability management;
- proper and comprehensive risk assessment and management;
- proper business and accounting and financial reporting functions, including proper authorisation, processing and recording of transactions;
- completeness, accuracy and timeliness of accounting records, managerial information, regulatory reports, etc.;
- reliability of IT-systems, data and systems integrity and protection;
- prevention of fraudulent or illegal activities, including misappropriation of assets;
- compliance with laws and regulations, including anti-money laundering and anti-corruption.

The internal control system in the Bank is implemented via following bodies and units:

- the general meeting of shareholders;
- the Board of Directors and its committees, including the Audit Committee;
- the Management Board and the Chairman of the Management Board;
- the Revision Commission;
- the Chief Accountant;
- the Risk Management function;
- the Credit Risk Management function;
- AML and CTF (Anti-Money Laundering and Counter Terrorist Financing);
- the Currency Control function;
- the Legal Expertise function;
- the Function of Internal Control of Bank's activities on the financial market;
- the Internal Control function;
- the Security function (including IT Security function);
- the Internal Audit function.

The Board of Directors is responsible for strategic supervision and control.

Bearing in mind the proposals of the Management Board, the Board of Directors establishes and approves:

- the business model, taking into account the risks to which this model exposes the Bank and the procedures for identifying and measuring these risks;
- the Bank's overall governance structure;
- the strategic guidelines and periodically reviews them due to changes in business activities and the external context, in order to ensure their ongoing effectiveness;
- the risk appetite, risk tolerance and risk governance policies;
- the guidelines of the internal control system, ensuring that it is in line with the stated strategic choices and risk appetite, and that it is able to take account of risk evolution and interaction;

(Thousands of Russian Roubles)

- the criteria for identifying the significant transactions to be subject to prior approval by the Risk Management function;
- the main points of the ICAAP (Internal Capital Adequacy Assessment Process), its coherence with the RAF (Risk Appetite Framework) and its prompt adaptation to significant changes in strategic policies, organisational arrangements and the business environment; takes steps to ensure the full use of the results of the ICAAP for strategic and decision-making purposes.

The Board of Directors establishes and approves:

- the Bank's organisational structure;
- the establishment of the corporate control functions, their tasks and responsibilities, the methods of coordination and collaboration, and information flows between these functions and between them and the corporate bodies;
- the risk management process, and assesses its compatibility with the strategic guidelines and risk governance policies;
- the accounting and reporting systems;
- the policies and processes for evaluating the Bank's assets, and in particular its financial instruments, ensuring their ongoing adequacy; it also establishes the Bank's maximum exposure limits to financial instruments or products whose valuation is uncertain or difficult;
- adoption of the internal risk measurement systems for the calculation of capital requirements. Specifically, it approves the selection of the system deemed suitable and a plan of activities for setting it up and implementing it, identifying responsibilities, specifying the timetable for implementation and the planned investment of human, financial and technological resources;
- the annual declaration of compliance with the requirements for using internal evaluation systems, taking a reasoned decision and examining all information from the validation function;
- the process for the development and validation of internal risk management systems not used for regulatory purposes, and periodically assessing their proper functioning.

The Board of Directors and the Management Board have responsibility for development, implementation and monitoring of internal control system.

The Board of Directors also assumes overall responsibility for managing and monitoring the IT system (including supervising the analysis of IT risk) and business continuity. It approves the programme of activities (including the audit plan) prepared, on at least an annual basis, by the Internal Audit function, and the multi-year audit plan.

The Management Board is responsible for contributing to strategic supervision and management. The Management Board contributes to strategic supervision functions regarding the internal control system, in line with the ISP Group Policy. The Management Board provides the Board of Directors with proposals on the appointment and removal of the managers of corporate control functions and the business continuity plan Manager.

The Management Board ensures integrated management of all business risks, evaluating the internal and external factors from which these risks may derive and their mutual interrelations. It is responsible for taking all necessary actions to ensure that the Bank and the internal control system comply with regulatory standards and requirements, monitoring their ongoing compliance. The Management Board manages the implementation of all strategic decisions; plans and manages implementation of the risk management process as well as implementation of processes relating to the praxis for the approval of new products or services; establishes the internal information flows necessary to ensure that the corporate bodies and control functions are fully apprised of and are able to manage risk factors and can verify compliance with the RAF; takes the necessary actions to ensure the ongoing comprehensiveness, adequacy, functionality and reliability of the internal control system; ensures that the risk management process is coherent with the risk appetite and risk governance policies and ensures correct, prompt and secure management of information for accounting, management and reporting purposes; ensures the comprehensiveness, adequacy, functionality and reliability of the IT system.

The Bank developed a system of standards, policies and procedures to ensure proper operations and compliance with relevant legal and regulatory requirements, including the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions;
- requirements for the recording, reconciliation and monitoring of transactions;
- compliance with regulatory and other legal requirements;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- requirements for the reporting of operational losses and proposed remedial action;
- development of contingency plans;
- training and professional development;
- ethical and business standards;

(Thousands of Russian Roubles)

- risk mitigation, including insurance where this is effective;
- rules on protection and confidentiality of information and control over compliance with the requirements of the Federal law on the insider information and market manipulation;
- procedure of access to the insider information.

The CBR sets out the specific requirements for the Internal Audit function and the Internal Control function. Based on above legal requirements the Internal Control function conducts compliance activities focused primarily on regulatory risks faced by the Bank.

The main functions of the Internal Control function include the following:

- identification of compliance risks and regulatory risks;
- monitoring of events related to regulatory risk, including probability of occurrence and quantitative assessment of its' consequences;
- monitoring of regulatory risk;
- preparation of recommendations on regulatory risk management;
- coordination and participation of design of measures to decrease regulatory risk;
- monitoring of efficiency of regulatory risk management;
- participation in preparation of internal documents on regulatory risk management, anti-corruption, compliance with corporate behaviour rules, code of professional ethics and minimisation of conflicts of interest;
- analysis of dynamics of clients' complaints;
- monitoring of compliance with the Russian legislation, the CBR requirements, self-regulated organisations, internal regulations, and correct accounting of securities transactions;
- maintaining the list of insiders;
- analysis of economic reasonableness of outsourcing agreements of Bank's services;
- participation in interaction with authorities, self-organised organisations, associations and financial market participants.

The main functions of the Internal Audit function include the following:

- audit and efficiency assessment of the system of internal control as a whole, fulfillment of the decisions of key management structures;
- audit of efficiency of methodology of assessment of banking risks and risk management procedures, regulated by internal documents in the Bank (methods, programmes, rules and procedures for banking operations and transactions, and for the management of banking risks);
- audit of reliability of internal control system over automated information systems;
- audit and testing of fairness, completeness and timeliness of accounting and reporting function and the reliability (including the trustworthiness, fullness and objectivity) of the collection and submission of financial information;
- audit of applicable methods of safekeeping the Bank's property;
- assessment of economic reasonability and efficiency of operations and other deals;
- audit of internal control processes and procedures;
- audit of the Internal Control function and the Risk Management function.

Compliance with ISP Group standards is supported by periodic reviews undertaken by the Internal Audit Division (further, "the Internal Audit function"). The Internal Audit function is independent from business operations and is subordinated to and reports to the Board of Directors. The results of the Internal Audit function reviews are discussed with relevant business process managers, with summaries submitted to the Audit Committee, the Board of Directors and senior management of the Bank and the ISP Group.

Russian legislation, including Federal Law dated 2 December 1990 No. 395-1 *On Banks and Banking Activity,* Direction of the CBR dated 1 April 2014 No. 3223-U *On Requirements to the Head of the Risk Management Service*, the Head of the Internal Control Service, the Head of the Internal Audit Service of the Credit Organisation, establishes the professional qualification, business reputation and other requirements for the members of the Board of Directors, the Management Board, the Head of the Internal Audit function, the Internal Control function and the Risk Management function and other key management personnel. All members of the Bank's governing and management bodies of the Bank comply with these requirements.

There is a hierarchy of requirements for the authorization of transactions depending on their size and complexity. A significant portion of operations are automated and the Bank has a system of automated controls to monitor risks.

(Thousands of Russian Roubles)

Management believes that the Bank complies with the CBR requirements in respect of risk management and internal control systems, including requirements covering the Internal Audit function, and that risk management and internal control systems are appropriate for the scale, nature and complexity of Bank's operations.

The Bank's internal documentation, establishing the procedures and methodologies for identifying and managing the Bank's significant credit, operational, market, interest rate, legal, liquidity and reputational risks, and for stress-testing was approved by the authorised management bodies of the Bank in accordance with regulations and recommendations issued by the CBR.

The Bank maintained a system for reporting on the Banks's significant credit, operational, market, interest rate, legal, liquidity and reputational risks, and on the Bank's capital.

The frequency and consistency of reports prepared by the Bank's Risk management and Internal Audit functions during 2017, which cover the Banks's credit, operational, market, interest rate, legal, liquidity and reputational risk management, was in compliance with the Bank's internal documentation. The reports included observations made by the Bank's Risk Management and Internal Audit functions as to their assessment of the effectiveness of the Bank's procedures and methodologies, and recommendations for improvement.

The Board of Directors and the Management Board of the Bank had responsibility for monitoring the Bank's compliance with risk limits and capital adequacy ratios as established by the Bank's internal documentation. With the objective of monitoring effectiveness of the Bank's risk management procedures and their consistent application during 2017 the Board of Directors and the Management Board of the Bank periodically discussed reports prepared by the risk management and Internal Audit functions, and considered proposed corrective actions.

Risk management

Risk is inherent in the Bank's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is essential to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Bank is exposed to credit risk, liquidity risk and market risk. Operational, business and other non-financial risks are also inherent in the Bank's activities.

Risk management is the process of identification, measurement and monitoring of risks faced by the Bank, conducted in accordance with its particular organisational and functional structure and established for the appropriate management of the risk appetite expressed by the shareholders.

The independent risk control process does not cover business risks such as changes in the environment, technology and industry. They are monitored through the Bank's strategic planning process.

The Bank has the Risk Management function which performs centralised risk management to preserve and enhance value for the shareholders. Risk management function is not subordinated to and does not report to divisions accepting relevant risks.

The Risk Management function is based on the following general principles:

- independence from the business lines;
- entity wide approach;
- coherence at all aggregation levels through the use of consistent measuring models;
- timing in providing the data to support the decision-making and control processes;
- timely analysis and identification of potential possibilities of excess of risk thresholds along with the establishment of the corresponding measures to minimize such possibilities;
- transparency in assessment methodologies and criteria on acceptable thresholds for each risk type in accordance with the established levels of decision making process;
- segregation of duties between the Board of Directors, Chief Executive Officer, divisions and departments.

The Risk Management function is not subordinated to and does not report to divisions accepting relevant risks.

The Bank calculates mandatory ratios on a daily basis in accordance with the requirement of the CBR.

These are considered fundamental principles of governance rules with reference to the characteristics of internal management and control systems.

(Thousands of Russian Roubles)

Risk management structure

There is a multilevel system established in the Bank for making decisions related to risk management. The Board of Directors performs a strategic risk management; however, tactical functions are performed by collegiate authorities and specific independent bodies responsible for managing and monitoring risks.

Board of Directors

The Board of Directors is responsible for the overall risk management process and for approving risk strategies, principles, methodologies for identifying and managing significant risks, as well as identifying risk appetite and setting the overall risk framework for limits and monitoring capital adequacy and stress-testing.

Management Board

The Management Board has the responsibility to define and monitor the risk management process within the Bank, including monitoring of risk appetite adherence, monitoring of risk limits and capital adequacy as established by the Bank's approved internal documentation. The Management Board also approved the methodologies for identifying and managing significant risks.

Financial Risks Committee

The Financial Risk Committee is responsible for the protection and allocation of the Bank's equity, it ensures the criteria and methods on risks' evaluation and control procedures to be compliant with ISP Group guidelines. It also manages the Bank's portfolio, regularly monitors and evaluates the structure of assets and liabilities, as well as off-balance sheet items, performs the approval of the terms of the new financial products or changes in the existing ones, performs the monitoring of established risk limits compliance (internal and external). The Financial Risks Committee ensures the decision making is performed in accordance with the Banks' policies and other internal documentation.

Credit and Problem Asset Committee

The Credit Committee is the superior credit approval authority in the Bank. It is responsible for the credit issuance and reapproval of lending conditions within the established limits by counterparty. It makes decisions on proposals made by business units taking into account risks evaluation on each of them. For credit exposures above certain limit the final approval has to be provided by the Credit Committee taking into consideration an opinion provided by the Credit Department of ISP Group.

The Problem Asset Committee assesses the quality of the credit portfolio and its trends, approves assets' classification, level of impairment allowance, performs an analysis of settlement strategies for impaired loans, and monitors collection process and its results.

Risk Management function

The Risk Management function is responsible for implementing and maintaining significant and other risk management procedures, for maintenance of acceptable risk level limited by risk appetite to ensure an independent control process, including preparation of reports which include observations made as to its assessment of the effectiveness of Bank's procedures and methodologies, and recommendations for improvement. The frequency and consistency of these reports is in compliance with the Bank's internal documentation.

Treasury Division

The Treasury Division is responsible for managing the Bank's assets and liabilities and their structure. It is also primarily responsible for funding and liquidity risk management.

Internal Audit function

Risk management processes are audited annually by the Internal Audit function. It reviews risk management policies and procedures and reports its findings, including the assessment of the effectiveness of the Bank's procedures and methodologies and recommendations for improvement, to the Audit Committee. The frequency and consistency of the reports is in compliance with the internal documentation. Based on the recommendations of the Audit Committee, the Board of Directors considers proposed corrective actions.

Risk measurement and reporting systems

Risk monitoring and controlling are primarily performed based on the established limits. These limits reflect the business strategy and market environment as well as the level of the risk that the Bank is willing to accept, with additional emphasis on selected industries. In addition, the Bank maintains the system for reporting related to the capital of the Bank, and monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risks types such as credit, operational, market, interest rate, legal, liquidity and reputational risks.

(Thousands of Russian Roubles)

Information compiled from all business units is examined and processed in order to analyse, control and identify risks. This information is reported to the Board of Directors, the Management Board, the Financial Risks Committee and the Credit Committee. The report is prepared quarterly and includes aggregate credit exposures, credit metric forecasts, hold limit exceptions, market risk exposures, liquidity ratios and risk profile changes. The Management Board analyses risk reports and where necessary reallocates risk limits to achieve target strategic risk profile. The reports of the Risk Management function are periodically discussed by the Board of Directors and the Management Board and proposed corrective actions are considered. The Risk Management function also is involved in process of Homogeneous Credit Risk Monitoring and Risk Appetite Framework leading by the International Subsidiaries Banks Division of the ISP Group.

Risk mitigation

As part of its overall risk management process, the Bank uses derivatives and other instruments to manage exposures resulting from changes in interest rates, foreign currencies, and exposures arising from forecasted transactions.

To reduce its credit risks, the Bank uses the number of instruments which allow from the one hand to minimize the occurrence of the credit risk event both on separate loans and homogeneous portfolio, and from the other hand to maximize the return when the credit risk event occurs.

Risk concentrations

Concentrations arise when a number of counterparties are engaged in similar business activities or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes of the same economic factors.

In order to avoid excessive concentrations of risks, the Bank's policies and procedures include specific guidelines to focus on, including maintaining diversified portfolios. The Bank takes measures to correct the excess of the established limits of identified concentrations of credit risks accordingly.

Credit risk

Credit risk is the risk of a financial loss to the Bank if a counterparty of a financial instrument fails to meet its contractual obligations.

The basic principles of credit risk management include:

- close connection between credit risk management system and strategic aims and tasks of the Bank;
- involvement of the Board of Directors and governing bodies of the Bank into credit risk management issues;
- overall identification, analysis and establishment of credit risk minimization system;
- follow-up control, regular monitoring and reporting.

The policies of the Bank within the credit procedures determine:

- procedures for review and approval of loan applications;
- methodology for the credit assessment of the borrowers (corporate and retail);
- methodology for the credit assessment of counterparties, issuers and insurance companies;
- methodology for the evaluation of collateral;
- credit documentation requirements;
- procedures for the ongoing monitoring of loans and other credit exposures.

Credit processes comprise the assessment of credit quality of counterparty and structuring the deal in terms of issued product; credit administration process and further control, including regular analysis of creditworthiness of customers, covenants check, analysis of contractual obligations, planned use of funds, etc; management of portfolio of homogeneous credit products.

Functions of the deal's initiation and evaluation of credit risks are separated. The Underwriting Department, being an independent division, performs primary and secondary analysis of a client in terms his business, financial situation, operational market, deal structure and compliance with the Bank's and ISP Group's policy. The Credit Committee makes the decision on the loan application on the basis of submissions by the Underwriting Department.

The Bank continuously monitors the performance of individual credit exposures and regularly reassesses the creditworthiness of its customers. The review is based on the customer's most recent financial statements and other information submitted by the customer, or otherwise obtained by the Bank. Apart from planned activities, the Bank also performs additional monitoring in case of any negative signs towards clients' business and financial situation. The credit portfolio is assessed by the Risk Management function with the reports being provided to executive bodies of the Bank and to the Board of Directors.

(Thousands of Russian Roubles)

The maximum exposure to credit risk is generally reflected in the carrying amounts of financial assets in the consolidated statement of financial position and unrecognised credit related commitment amounts. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

In accordance with the requirements of the CBR, the Bank also calculates on a daily basis mandatory maximum risk exposure ratio per borrower or group of related borrowers (N6), which regulates (mitigates) the Bank’s credit risk in respect of a borrower or group of related borrowers and sets the maximum ratio of the total liabilities of a borrower (borrowers within a group of related borrowers) owed to the Bank, to the Bank's own funds (capital). As at 31 December 2017 and 2016, the maximum level of N6 ratio set by the CBR was 25.0%. The N6 ratio calculated by the Bank as at 31 December 2017 was 18.6% (2016: 19.1%) and was in compliance with limits set by the CBR.

Derivative financial instruments

Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values, as recorded in the consolidated statement of financial position.

Credit related commitments

The Bank provides financial guarantees and letters of credit to its customers which may require the Bank to make payments on their behalf. Such payments are further collected from customers based on the terms of financial guarantees and letters of credit. They expose the Bank to credit risk and are mitigated by the same credit risk management policies and procedures.

The credit quality of loans to customers and net investments in financial leases is managed using internal classification.

(Thousands of Russian Roubles)

The following table shows the information on the credit quality of loans to customers and net investments in financial leases based on this classification as at 31 December.

	2017				*2016*			
	Gross loans	*Impairment allowance*	*Net loans*	*Impairment allowance to gross loans, %*	*Gross loans*	*Impairment allowance*	*Net loans*	*Impairment allowance to gross loans, %*
Loans to corporate customers								
Loans to large corporate customers								
Neither past due nor impaired	**12 467 761**	**(279 616)**	**12 188 145**	**2.2**	**12 651 133**	**(377 389)**	**12 273 744**	**3.0**
Impaired loans:	**3 052 562**	**(2 289 745)**	**762 817**	**75.0**	**4 775 424**	**(3 678 962)**	**1 096 462**	**77.0**
- past due less than 90 days	1 710 640	(1 111 756)	598 884	65.0	1 906 977	(1 029 071)	877 906	54.0
- past due more than 90 days but less than 1 year	220 186	(156 921)	63 265	71.3	919 301	(808 341)	110 960	87.9
- past due more than 1 year	1 121 736	(1 021 068)	100 668	91.0	1 949 146	(1 841 550)	107 596	94.5
Total loans to large corporate customers	**15 520 323**	**(2 569 361)**	**12 950 962**	**16.6**	**17 426 557**	**(4 056 351)**	**13 370 206**	**23.3**
Loans to small and medium corporate customers								
Neither past due nor impaired	**12 794 004**	**(164 768)**	**12 629 236**	**1.3**	**13 602 784**	**(154 178)**	**13 448 606**	**1.1**
Past due but not impaired:	**21 138**	**(2 648)**	**18 490**	**12.5**	**199 927**	**(25 246)**	**174 681**	**12.6**
- past due less than 90 days	21 138	(2 648)	18 490	12.5	199 927	(25 246)	174 681	12.6
Impaired loans:	**3 270 760**	**(1 635 815)**	**1 634 945**	**50.0**	**4 008 550**	**(2 062 368)**	**1 946 182**	**51.4**
- past due less than 90 days	317 195	(93 224)	223 971	29.4	557 670	(197 597)	360 073	35.4
- past due more than 90 days but less than 1 year	453 681	(180 398)	273 283	39.8	720 685	(357 020)	363 665	49.5
- past due more than 1 year	2 499 884	(1 362 193)	1 137 691	54.5	2 730 195	(1 507 751)	1 222 444	55.2
Total loans to small and medium corporate customers	**16 085 902**	**(1 803 231)**	**14 282 671**	**11.2**	**17 811 261**	**(2 241 792)**	**15 569 469**	**12.6**
Total loans to corporate customers	**31 606 225**	**(4 372 592)**	**27 233 633**	**13.8**	**35 237 818**	**(6 298 143)**	**28 939 675**	**17.9**
Loans to retail customers								
Neither past due nor impaired	**1 678 255**	**(11 828)**	**1 666 427**	**0.7**	**1 513 037**	**(13 716)**	**1 499 321**	**0.9**
Past due but not impaired:	**35 649**	**(7 011)**	**28 638**	**19.7**	**30 751**	**(7 046)**	**23 705**	**22.9**
- past due less than 90 days	35 649	(7 011)	28 638	19.7	30 751	(7 046)	23 705	22.9
Impaired loans:	**193 444**	**(127 054)**	**66 390**	**65.7**	**202 689**	**(127 739)**	**74 950**	**63.0**
- past due less than 90 days	34 604	(13 842)	20 762	40.0	39 139	(19 114)	20 025	48.8
- past due more than 90 days but less than 1 year	24 731	(18 751)	5 980	75.8	42 840	(27 761)	15 079	64.8
- past due more than 1 year	134 109	(94 461)	39 648	70.4	120 710	(80 864)	39 846	67.0
Total loans to retail customers	**1 907 348**	**(145 893)**	**1 761 455**	**7.6**	**1 746 477**	**(148 501)**	**1 597 976**	**8.5**
Total loans to customers	**33 513 573**	**(4 518 485)**	**28 995 088**	**13.5**	**36 984 295**	**(6 446 644)**	**30 537 651**	**17.4**
Net investments in finance leases								
Neither past due nor impaired	**1 304 753**	**(20 738)**	**1 284 015**	**1.6**	**915 634**	**(13 065)**	**902 569**	**1.4**
Past due but not impaired:	**17 422**	**(1 967)**	**15 455**	**11.3**	**40 117**	**(7 287)**	**32 830**	**18.2**
- past due less than 90 days	17 422	(1 967)	15 455	11.3	38 779	(6 994)	31 785	18.0
- past due more than 90 days but less than 1 year	-	-	-	-	1 338	(293)	1 045	21.9
Impaired:	**106 538**	**(71 891)**	**34 647**	**67.5**	**140 489**	**(77 711)**	**62 778**	**55.3**
- past due less than 90 days	16 558	(3 925)	12 633	23.7	53 798	(15 099)	38 699	28.1
- past due more than 90 days but less than 1 year	7 840	(3 902)	3 938	49.8	20 726	(10 079)	10 647	48.6
- past due more than 1 year	82 140	(64 064)	18 076	78.0	65 965	(52 533)	13 432	79.6
Total net investments in finance leases	**1 428 713**	**(94 596)**	**1 334 117**	**6.6**	**1 096 240**	**(98 063)**	**998 177**	**8.9**

(Thousands of Russian Roubles)

Key assumptions and judgments for estimating the loan impairment

The Bank estimates loan impairment for impaired loans to corporate clients, net investments in finance leases and retail customers based on an analysis of the future cash flows. In determining the impairment allowance management assumes a delay in obtaining proceeds from the foreclosure of collateral and discounts the estimated fair value of collateral based on the type of asset.

The Bank estimates loan impairment for loans to corporate clients, net investments in finance leases and retail customers for which no evidence of impairment has been identified based on its internal model (acceptable proxy of ISP requirements) which takes into account historical loss experience for each type of loan.

To determine the amount of the impairment allowance for loans assessed collectively management makes the assumption that loss migration rates are constant and can be estimated based on the historic loss migration pattern (2 years).

The key inputs to loss rates are probability of default (PD) and loss given default (LGD). These indicators are calculated by the Bank based on its own historic experience and statistics.

Changes in these estimates could affect the loan impairment allowance. For example, to the extent that the net present value of the estimated cash flows differs by plus/minus three percent, the impairment allowance on loans to corporate clients, net investments in finance leases and retail customers as at 31 December 2017 would be RUB 817 009 thousand, RUB 40 024 thousand, RUB 52 844 thousand, respectively lower/higher (2016: RUB 868 190 thousand, RUB 29 945 thousand and RUB 47 939 thousand).

In determining the impairment allowance for guarantees issued and letters of credit management uses the same loss migration rates as for loans to customers.

Analysis of collateral and other credit enhancements

The probability of the return of the lended amounts to the Bank mainly depends on creditworthiness of a client rather than on a collateral value. Nevertheless the existence of additional sources of repayment makes the important role in credit risks minimization.

The Bank accepts different types of assets as collateral for loans to customers in order to minimize its' credit risks. The Bank takes collateral classified as being the 1st class (e.g. guarantees) and standard, depending on its' quality and liquidity, following the internal methodology.

The Bank has procedures for monitoring the fair value of collateral, which include requesting for additional collateral in case the current value of collateral declines. Fair value of the collateral is reviewed within the periodicity determined in the Collateral Policy of the Bank.

During the year ended 31 December 2017, the Bank obtained certain assets by taking possession of collateral for loans to customers and net investments in finance leases. As at 31 December 2017, the carrying amount of such assets is RUB 194 854 thousand (2016: RUB 207 738 thousand), which consisted of real estate of RUB 186 379 thousand (2016: RUB 200 408 thousand) and other assets of RUB 8 475 thousand (2016: RUB 7 330 thousand). The Bank's policy is to dispose of these assets as soon as it is practicable.

(Thousands of Russian Roubles)

The following tables provide information on collateral and other credit enhancements securing loans to customers, net of impairment, by types of collateral or other credit enhancement as at 31 December.

2017

	Real estate	*Motor vehicles*	*Equipment*	*Guarantees*	*Total collateralised loans*	*Total not collateralised loans*	*Total loans to customers*
Loans to corporate customers							
Loans to large corporate customers							
Neither past due nor impaired	953 352	294 793	940 999	237 379	2 426 523	9 761 622	12 188 145
Impaired loans	624 966	-	-	-	624 966	137 851	762 817
Total loans to large corporate customers	**1 578 318**	**294 793**	**940 999**	**237 379**	**3 051 489**	**9 899 473**	**12 950 962**
Loans to small and medium customers							
Neither past due nor impaired	8 121 572	953 913	700 341	-	9 775 826	2 853 410	12 629 236
Past due but not impaired	10 638	272	253	-	11 163	7 327	18 490
Impaired loans	1 376 849	140 528	57 646	-	1 575 024	59 922	1 634 945
Total loans to small and medium corporate customers	**9 509 059**	**1 094 713**	**758 240**	**-**	**11 362 012**	**2 920 659**	**14 282 671**
Total corporate customers	**11 087 377**	**1 389 506**	**1 699 239**	**237 379**	**14 413 501**	**12 820 132**	**27 233 633**
Loans to retail customers							
Neither past due nor impaired	496 763	-	-	-	496 763	1 169 664	1 666 427
Past due but not impaired	12 359	-	-	-	12 359	16 279	28 638
Impaired loans	61 991	-	-	-	61 991	4 399	66 390
Total loans to retail customers	**571 113**	**-**	**-**	**-**	**571 113**	**1 190 342**	**1 761 455**
Total loans to customers	**11 658 490**	**1 389 506**	**1 699 239**	**237 379**	**14 984 614**	**14 010 474**	**28 995 088**
Net investments in finance lease							
Neither past due nor impaired	9 274	715 661	549 051	-	1 273 986	10 029	1 284 015
Past due but not impaired	-	8 236	7 219	-	15 455	-	15 455
Impaired loans	-	6 396	25 806	-	32 202	2 445	34 647
Total net investments in finance leases	**9 274**	**730 293**	**582 076**	**-**	**1 321 643**	**12 474**	**1 334 117**

(Thousands of Russian Roubles)

	Real estate	*Motor vehicles*	*Equipment*	*Guarantees*	*Total collateralised loans*	*Total not collateralised loans*	*Total loans to customers*
				2016			
Loans to corporate customers							
Loans to large corporate customers							
Neither past due nor impaired	747 330	911 459	1 117 933	110 704	2 887 426	9 386 318	12 273 744
Impaired loans	687 083	30 782	15 568	-	733 433	363 029	1 096 462
Total loans to large corporate customers	**1 434 413**	**942 241**	**1 133 501**	**110 704**	**3 620 859**	**9 749 347**	**13 370 206**
Loans to small and medium corporate customers							
Neither past due nor impaired	8 735 145	1 431 177	725 369	-	10 891 691	2 556 915	13 448 606
Past due but not impaired	127 266	31 364	3 149	-	161 779	12 902	174 681
Impaired loans	1 485 078	217 451	131 756	-	1 834 285	111 897	1 946 182
Total loans to small and medium corporate customers	**10 347 489**	**1 679 992**	**860 274**	**-**	**12 887 755**	**2 681 714**	**15 569 469**
Total loans corporate customers	**11 781 902**	**2 622 233**	**1 993 775**	**110 704**	**16 508 614**	**12 431 061**	**28 939 675**
Loans to retail customers							
Neither past due nor impaired	533 955	-	-	-	533 955	965 366	1 499 321
Past due but not impaired	5 982	-	-	-	5 982	17 723	23 705
Impaired loans	74 125	-	-	-	74 125	825	74 950
Total loans to retail customers	**614 062**	**-**	**-**	**-**	**614 062**	**983 914**	**1 597 976**
Total loans to customers	**12 395 964**	**2 622 233**	**1 993 775**	**110 704**	**17 122 676**	**13 414 975**	**30 537 651**
Net investments in finance lease							
Neither past due nor impaired	11 775	420 978	456 323	-	889 076	13 493	902 569
Past due but not impaired	-	23 963	8 391	-	32 354	476	32 830
Impaired loans	-	5 188	52 556	-	57 744	5 034	62 778
Total net investments in finance leases	**11 775**	**450 129**	**517 270**	**-**	**979 174**	**19 003**	**998 177**

(Thousands of Russian Roubles)

The tables above are presented on the basis of fair value of collateral as described below excluding over collateralisation.

For loans secured by multiple types of collateral, collateral that is most relevant for impairment assessment is disclosed. Guarantees and sureties received from individuals, such as shareholders of SME borrowers, are not considered for impairment assessment purposes.

The recoverability of loans which are not impaired or past due is primarily dependent on the creditworthiness of the borrowers rather than the value of collateral, and the Bank does not necessarily update the valuation of collateral performed at the loan inception date as at each reporting date.

For impaired, past due and other certain loans the fair value of collateral is updated with frequency defined in the Collateral Policy.

Mortgage loans to individuals are secured by the underlying housing real estate. The Bank's policy is to issue mortgage loans with a loan-to-value ratio of a maximum of 80%.

For certain mortgage loans the Bank updates the appraised values of collateral obtained at inception of the loan to the current values considering the approximate changes in property values. The Bank may also obtain a specific individual valuation of collateral at each reporting date where there are indications of impairment. For the remaining mortgage loans the fair value of collateral was estimated at inception of the loans and was not adjusted for subsequent changes to the reporting date.

Geographical concentration

The geographical concentration of assets and liabilities as at 31 December 2017 is as follows:

	Russia	*OECD*	*CIS and other countries*	*Total*
Assets				
Cash and cash equivalents	2 733 411	1 143 162	9 722	3 886 295
Mandatory cash balances with the Central Bank of the Russian Federation	298 979	-	-	298 979
Amounts due from credit institutions	9 402 079	2 728 577	1 398 081	13 528 737
Available-for-sale securities:				
- held by the Bank	4 130 899	-	-	4 130 899
Loans to customers:	28 416 340	2 809	575 939	28 995 088
-loans to large corporate customers	*12 375 403*	*-*	*575 559*	*12 950 962*
-loans to small and medium customers	*14 282 671*	*-*	*-*	*14 282 671*
-loans to retail customers	*1 758 266*	*2 809*	*380*	*1 761 455*
Net investments in finance leases	1 334 117	-	-	1 334 117
Property and equipment	1 131 217	-	-	1 131 217
Intangible assets	585 667	-	-	585 667
Deferred income tax assets	328 348	-	-	328 348
Other assets	848 216	24 697	1 490	874 403
Total assets	**49 209 273**	**3 899 245**	**1 985 232**	**55 093 750**
Liabilities				
Amounts due to credit institutions	4 920 195	958 310	6 145	5 884 650
Amounts due to customers:	28 191 123	2 201 405	134 577	30 527 105
-legal entities, state and non-profit organisations	*12 399 817*	*1 290 055*	*10 831*	*13 700 703*
-individuals	*15 791 306*	*911 350*	*123 746*	*16 826 402*
Debt securities issued	3 186 066	-	-	3 186 066
Other liabilities	691 326	24 318	30 868	746 512
Subordinated debt	-	2 304 839	-	2 304 839
Total liabilities	**36 988 710**	**5 488 872**	**171 590**	**42 649 172**
Net position	**12 220 563**	**(1 589 627)**	**1 813 642**	**12 444 578**
Credit related commitments	**13 555 553**	**86 395**	**4 032 288**	**17 674 236**

(Thousands of Russian Roubles)

Assets, liabilities and credit related commitments are allocated based on the country in which the counterparty performs its business activities. Cash on hand and property and equipment are allocated based on the country in which they are physically held. The Bank's operations include transactions with counterparties that operate in OECD countries, primarily Italy, Luxemburg, Germany, United States and United Kingdom.

The geographical concentration of assets and liabilities as at 31 December 2016 is as follows:

	Russia	*OECD*	*CIS and other countries*	*Total*
Net position	**15 347 951**	**(4 028 540)**	**737 980**	**12 057 391**
Credit related commitments	**9 631 134**	**386 147**	**4 246 608**	**14 263 889**

Liquidity risk

Liquidity risk is the risk of a potential loss arising in case the Bank is unable to meet its financial obligations as they fall due.

Liquidity risk exists when maturities of assets and liabilities do not match. The matching and/or controlled mismatching of maturities and interest rates of assets and liabilities is fundamental to liquidity management. It is unusual for financial institutions ever to be completely matched since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

The Bank maintains liquidity management with the objective to ensure that funds will be available at all times to honor all cash flow obligations as they become due. The liquidity policy is reviewed and approved by the Board of Directors.

The Treasury Division performs the daily liquidity management in line with the Policy on liquidity risk management established in the Bank. It performs its' activity to comply with the structured ratios and liquidity ratios of the CBR and ISP Group. When performing operating activity on liquidity management, the Treasury Division maintains the volume of liquid assets portfolio of the Bank at the required level, and uses the interbank istruments to optimize the structure of the Bank's balance.

The Risk Management function perfroms daily monitoring of liquidity position and perfroms stress-testing on a regular basis, taling into consideration possible scenarios of market conditions, both at normal and unfavourable level.

The liquidity position is also assessed and managed by the Bank, based on certain liquidity ratios calculated on a daily basis in accordance with the requirements of the CBR. The following table shows the mandatory liquidity ratios calculated as at 31 December 2017 and 2016.

As at 31 December, these ratios are as follows:

	Requirement	*2017, %*	*2016, %*
Instant Liquidity Ratio (N2)	Not less than 15%	58.7	73.9
Current Liquidity Ratio (N3)	Not less than 50%	112.4	88.9
Long-Term Liquidity Ratio (N4)	Not more than 120%	61.4	41.9

The Bank also regularly monitors Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR), established by the requirements of the Basel III.

The table below shows the structure of assets and liabilities as at 31 December 2017 in accordance with their contractual maturity.

Included in overdue loans to customers are wholly overdue loans and partially overdue loans but only in the amount of overdue payments.

(Thousands of Russian Roubles)

	On demand	*Less than 1 month*	*From 1 to 3 months*	*From 3 months to 1 year*	*From 1 to 5 years*	*Over 5 years*	*Overdue or no stated maturity*	*Total*
Assets								
Cash and cash equivalents	3 886 295	-	-	-	-	-	-	3 886 295
Mandatory cash balances with the Central Bank of the Russian Federation	121 374	31 084	34 336	100 354	11 831	-	-	298 979
Amounts due from credit institutions	-	13 528 737	-	-	-	-	-	13 528 737
Available-for-sale securities:								
- held by the Bank	-	4 130 899	-	-	-	-	-	4 130 899
Loans to customers	-	1 722 770	3 014 125	10 242 102	10 400 594	1 104 217	2 511 280	28 995 088
Net investments in finance leases	-	57 288	118 098	451 622	657 007	-	50 102	1 334 117
Property and equipment	-	-	-	-	-	-	1 131 217	1 131 217
Intangible assets	-	-	-	-	-	-	585 667	585 667
Deferred income tax assets	-	-	-	-	-	-	328 348	328 348
Other assets	125 455	101 423	269 893	137 059	44 787	457	195 329	874 403
Total assets	**4 133 124**	**19 572 201**	**3 436 452**	**10 931 137**	**11 114 219**	**1 104 674**	**4 801 943**	**55 093 750**
Liabilities								
Amounts due to credit institutions	970 502	3 381 298	-	57 569	1 475 281	-	-	5 884 650
Amounts due to customers	12 392 827	3 173 815	3 505 884	10 246 598	1 207 981	-	-	30 527 105
incl. amounts due to individuals	*2 027 448*	*1 461 635*	*2 230 604*	*9 975 953*	*1 130 762*	*-*	*-*	*16 826 402*
Debt securities issued	-	-	-	131 523	3 054 543	-	-	3 186 066
Other liabilities	138 433	25 960	233 763	237 922	57 777	14 987	37 670	746 512
Subordinated debt	-	-	-	-	2 304 839	-	-	2 304 839
Total liabilities	**13 501 762**	**6 581 073**	**3 739 647**	**10 673 612**	**8 100 421**	**14 987**	**37 670**	**42 649 172**
Net position	**(9 368 638)**	**12 991 128**	**(303 195)**	**257 525**	**3 013 798**	**1 089 687**	**4 764 273**	**12 444 578**
Accumulated gap as at 31 December 2017	**(9 368 638)**	**3 622 490**	**3 319 295**	**3 576 820**	**6 590 618**	**7 680 305**	**12 444 578**	
Accumulated gap as at 31 December 2016	**(9 926 281)**	**(434 905)**	**836 812**	**6 500 460**	**8 596 020**	**6 888 041**	**12 057 391**	

In the Russian marketplace, many short-term credits are granted with the expectation of renewing the loans at maturity. As such, the ultimate maturity of assets may be different from the analysis presented above.

Available-for-sale securities represented by Russian State bonds (OFZ), the CBR bonds (“KOBR”) are classified in the category “Less than 1 month” as they are considered to be highly liquid financial instruments.

Overdue liabilities, such as term deposits not withdrawn by the customers, are classified within the “On demand” category.

Debt securities are reflected by the date of the offer and not the final maturity date (as at 31 December 2017 there are no offer date before the maturity date for debt securities issued).

Unused vacations in the amount of RUB 49 807 thousand are classified into the category “from 3 months to 1 year” in accordance with the Bank’s judgement based on historical pattern.

Mandatory cash balances with the CBR are allocated between the different maturity categories in accordance with the maturities of the liabilities to which they relate.

In case of necessity accumulated gap in the category “on demand” could be managed by attracting funds from ISP Group.

(Thousands of Russian Roubles)

The maturity profile of financial liabilities and credit related commitments as at 31 December 2017 based on contractual undiscounted repayment obligations is as follows:

	On demand	*Less than 1 month*	*From 1 to 3 months*	*From 3 months to 1 year*	*From 1 to 5 years*	*Over 5 years*	*Total*	*Carrying amount*
Financial liabilities								
Amounts due to credit institutions	970 502	3 395 428	16 574	130 788	1 610 772	-	**6 124 064**	**5 884 650**
Amounts due to customers	12 392 827	3 184 606	3 544 740	10 627 981	1 250 554	-	**31 000 708**	**30 527 105**
incl. amounts due to individuals	*2 027 448*	*1 467 383*	*2 255 899*	*10 355 355*	*1 171 620*	-	***17 277 705***	***16 826 402***
Debt securities issued	-	-	-	427 766	3 291 720	-	**3 719 486**	**3 186 066**
Other liabilities	-	-	199 311	24 860	-	-	**224 171**	**224 171**
Subordinated debt	-	12 634	25 267	113 703	2 911 254	-	**3 062 858**	**2 304 839**
Total financial liabilities	**13 363 329**	**6 592 668**	**3 785 892**	**11 325 098**	**9 064 300**	**-**	**44 131 287**	**42 126 831**
Credit related commitments	**17 674 236**	-	-	-	-	-	**17 674 236**	**17 674 236**

The maturity profile of financial liabilities and credit related commitments as at 31 December 2016 based on contractual undiscounted repayment obligations is as follows:

	On demand	*Less than 1 month*	*From 1 to 3 months*	*From 3 months to 1 year*	*From 1 to 5 years*	*Over 5 years*	*Total*	*Carrying amount*
Financial liabilities								
Amounts due to credit institutions	2 095 961	26 620	2 933 144	118 705	2 088 374	14 706	**7 277 510**	**6 860 745**
Amounts due to customers	11 825 469	8 444 226	2 799 109	4 888 329	233 487	52 000	**28 242 620**	**27 965 071**
incl. amounts due to individuals	*1 670 600*	*960 111*	*2 346 259*	*4 515 216*	*192 595*	-	***9 684 781***	***9 477 458***
Debt securities issued	-	-	-	2 301 073	3 583 440	-	**5 884 513**	**4 875 106**
Other liabilities	-	-	283 946	-	-	-	**283 946**	**283 946**
Subordinated debt	-	13 304	26 608	119 737	638 596	2 754 759	**3 553 004**	**2 426 712**
Derivative financial instruments								
- inflow	-	*(1 912 495)*	*(1 276 908)*	-	-	-	***(3 189 403)***	***(1 735)***
- outflow	-	*1 913 091*	*1 275 363*	-	-	-	***3 188 454***	***786***
Total financial liabilities	**13 921 430**	**8 484 150**	**6 042 807**	**7 427 844**	**6 543 897**	**2 821 465**	**45 241 593**	**42 411 580**
Credit related commitments	**14 263 889**	-	-	-	-	-	**14 263 889**	**14 263 889**

The total gross inflow and outflow disclosed in the tables above is the contractual, undiscounted cash flow on the financial liability or commitment.

In accordance with the Russian Civil Code, the Bank is obliged to repay time deposits to individuals upon demand of a depositor. In the tables above these deposits are classified in accordance with their stated maturity and are disclosed by each time band.

(Thousands of Russian Roubles)

Market risk

Market risk is the risk that the fair value of assets or future cash flows of financial instruments will diminish due to changes in the interest rates, currency rates and equity prices. Market risk includes currency risk, interest rate risk and other price risks.

Market risks arises from open positions in interest rate, currency and equity financial instruments, which are exposed to general and specific market movements.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters whilst optimizing the return of risk.

Overall authority for market risk is vested in the Financial Risks Committee. Market risk limits are approved by the Board of Directors based on recommendations of the Risk Management function and the Financial Risks Committee.

The Bank manages its market risk by setting open positions and other limits in relation to financial instruments, which include acceptable level of positions (nominal and market ones), Value at Risk (“VaR”), PV100 and stop-loss limits, limits on open positions. These are monitored on a regular basis and reviewed and approved by the Management Board and the Board of Directors.

Market risk – Trading and AFS positions

The Bank applies a VaR methodology to assess the market risk positions held and to estimate the potential economic loss based upon a number of parameters and assumptions for various changes in market conditions. VaR is a technique that estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence. The VaR model used by the Bank is based upon a 99 percent confidence level and assumes a 1-day holding period.

For the purposes of interest rate risk calculations for fixed income securities the information on interest rates volatility and correlation is received from the ISP Group on a daily basis.

Although VaR is a valuable tool in measuring risk exposures, it has a number of limitations:

- the use of historical data as a basis for determining future events may not encompass all possible scenarios, particularly those that are of an extreme nature;
- a 1-day holding period assumes that all positions can be liquidated or hedged within that period. This is considered to be a realistic assumption in almost all cases but may not be the case in situations in which there is severe market illiquidity for a prolonged period;
- the use of a 99% confidence level does not take into account losses that may occur beyond this level. There is a one percent probability that the loss could exceed the VaR estimate;
- VaR is only calculated on the end-of-day balances and does not necessarily reflect exposures that may arise on positions during the trading day;
- the VaR measure is dependent upon the position and the volatility of market prices. The VaR of an unchanged position reduces if market volatility declines and vice versa.

To determine the reliability of the VaR model, actual outcomes are monitored regularly to test the validity of the assumptions and the parameters used in the VaR model. Market risk positions are also subject to regular stress tests to ensure that the Bank would withstand an extreme market event.

VaR limits have been established for available-for-sale portfolio, and exposure is calculated and monitored daily against the limits set by the Board of Directors. As at 31 December 2017, VaR for available-for-sale portfolio is RUB 1 366 thousand (2016: RUB 1 136 thousand).

Market risk – Non-Trading positions

Interest rate risk

Interest rate risk is the risk of a potential loss due to adverse changes in the market interest rates affecting the assets, liabilities and unrecognised positions sensitive to such changes.

Interest rate risk includes the following:

- Repricing Risk - the risk linked to the time differences in maturities (for fixed rate positions) and in the repricing dates (for floating rate positions);
- Yield Curve Risk - the risk linked to changes in the slope and shape of the yield curve;
- Basis Risk - the risk linked to the mismatch in the rates to be received and paid on different instruments, with similar repricing characteristics. When interest rates change, these differences can give rise to unexpected changes in the

(Thousands of Russian Roubles)

cash flows and interest margins for assets, liabilities and unrecognised positions with similar maturities or repricing frequencies.

The Bank uses the following methods to measure interest rate risk:

Sensitivity of the Fair Value measures the changes in the fair value of assets, liabilities and unrecognised positions resulting from a parallel rise in the discount curves by 100 b.p. To calculate the fair value, the discount curves which are suitable for measuring individual financial instruments are applied.

An analysis of sensitivity of the fair value as at 31 December is as follows:

Currency	*2017*	*2016*
RUB	(163 357)	(76 769)
USD	89 972	145 138
EUR	(2 189)	(4 382)
Total	**(75 574)**	**63 987**

A parallel fall in the discount curves by 100 b.p. would have had the equal but opposite effect on the fair value of assets, liabilities and unrecognised positions.

Sensitivity of the Interest Margin measures a one-year impact on the interest margin resulting from a parallel rise of the interest rate curves by 100 b.p. This measure highlights the effect of changes in interest rates on the portfolio being divided into current and term products excluding assumptions on future changes in the structure of assets and liabilities. Therefore, it cannot be considered as a predictor of the future levels of the interest margin.

An analysis of sensitivity of the interest margin as at 31 December is as follows.

Currency	*2017*	*2016*
RUB	33 985	19 104
USD	23 189	27 585
EUR	1 480	(1 995)
Total	**58 654**	**44 694**

The Bank is exposed to interest rate risk, principally as a result of lending at fixed interest rates, in amounts and for periods, which differ from those of term borrowings at floating interest rates. In practice, interest rates are generally fixed on a short-term horizon. To reduce the interest rate risk the Bank includes in its loan contracts a clause providing for a change in the interest rate in the event of a significant change in the market interest rates. Additionally, interest rates for long-term loans in foreign currencies are linked to LIBOR and EURIBOR.

The Board of Directors sets limits on the potential loss from interest rate risk that may be undertaken. These limits are regularly monitored.

(Thousands of Russian Roubles)

Currency risks

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in foreign exchange rates. Open currency positions limits, set by the CBR, are monitored on a daily basis The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2017 and 31 December 2016:

	RUB	*USD*	*EUR*	*Other currencies*	*Total*
Assets					
Cash and cash equivalents	2 417 821	447 657	1 005 827	14 990	3 886 295
Mandatory cash balances with the Central Bank of the Russian Federation	298 979	-	-	-	298 979
Amounts due from credit institutions	10 402 498	1 728 158	1 398 081	-	13 528 737
Available-for-sale securities:					
- held by the Bank	4 130 899	-	-	-	4 130 899
Loans to customers	24 610 602	2 793 895	1 590 591	-	28 995 088
Net investments in finance leases	1 333 207	-	910	-	1 334 117
Property and equipment	1 131 217	-	-	-	1 131 217
Intangible assets	585 667	-	-	-	585 667
Deferred income tax assets	328 348	-	-	-	328 348
Other assets	801 464	55 034	15 701	2 204	874 403
Total assets	**46 040 702**	**5 024 744**	**4 011 110**	**17 194**	**55 093 750**
Liabilities					
Amounts due to credit institutions	5 884 650	-	-	-	5 884 650
Amounts due to customers	24 406 077	2 703 582	3 405 671	11 775	30 527 105
Debt securities issued	3 186 066	-	-	-	3 186 066
Other liabilities	549 351	164 832	15 872	16 457	746 512
Subordinated debt	-	2 304 839	-	-	2 304 839
Total liabilities	**34 026 144**	**5 173 253**	**3 421 543**	**28 232**	**42 649 172**
Net recognised position	**12 014 558**	**(148 509)**	**589 567**	**(11 038)**	**12 444 578**
Net unrecognised position	**-**	**-**	**-**	**-**	**-**
Credit related commitments	**5 076 124**	**11 903 545**	**511 093**	**183 474**	**17 674 236**

The exposure to currency risk as at 31 December 2016 is as follows:

	RUB	*USD*	*EUR*	*Other currencies*	*Total*
Net recognised position	**12 905 756**	**403 981**	**(1 255 724)**	**3 378**	**12 057 391**
Net unrecognised position	**(711 982)**	**(564 240)**	**1 276 222**	**-**	**-**
Credit related commitments	**4 946 253**	**8 292 981**	**1 024 655**	**-**	**14 263 889**

The net unrecognised position represents the notional currency position on deliverable forward and spot foreign exchange contracts outstanding as at 31 December 2016. As the borrowings in foreign currencies from international financial institutions represent a significant part of the Bank's liabilities, it is the Bank's policy to effectively hedge against risks associated with its net currency position. Such activities do not qualify as hedging relationships in accordance with IFRS.

The Bank has loans to customers denominated in foreign currencies. Depending on the revenue sources of the borrower, the appreciation of the currencies against the RUB may adversely affect the borrowers' repayment ability and therefore increases the likelihood of future loan losses.

(Thousands of Russian Roubles)

The following table indicates the currencies to which the Bank had significant exposure at 31 December 2017 and 2016 on its non-trading positions and foreign currency derivatives. The analysis calculates the effect of a reasonably possible movement of the currency rates against the RUB, with all other variables held constant on the profit or loss and equity before income tax expense.

Currency	***2017***	***2016***
10% appreciation of USD against RUB	(14 851)	(16 026)
10% appreciation of EUR against RUB	58 957	2 050
Total	**44 106**	**(13 976)**

Operational risk

Operational risk is the risk of direct or indirect losses arising from failures in internal processes, human errors, IT systems and technical failures or external events. This definition includes legal risk but does not include strategic and reputation risks.

For managing operational risk the Bank follows operational risk guidelines and methodology of the CBR and ISP Group in compliance with Basel recommendations as well as locally-developed methodologies and tools. The Bank, in accordance with the ISP Group's requirements and the regulatory suggestions, developed an operational risk framework consisting of operational risk policy, self-testing and the process of monitoring of key operational risk indicators in order to perform an effective operational risk management and support the Bank's business.

Operational risk management is a structured system of processes, functions, responsibilities and resources aimed at detection and monitoring, assessment, minimization and control of operational risks, as well as providing their effective prevention in accordance with the requirements of the ISP Group and external legislation. Operational risk management is directly connected with the level of corporate governance and corporate ethics of the Bank.

The calculation of operational risk level is maintained in accordance with the CBR requirements.

The Bank applies the following methods to minimize the risk:

- establishing regulations of performing all key operations in terms of internal documentation;
- accounting and documenting the operations, including the data checks in initial documentation with operation accounts;
- segregation of duties, double check principle, setting of limits on operations;
- automation of operations;
- control over the access to the information, multi-level security of data;
- taking measures on ensuring going concern when doing banking operations and deals;
- hedging of operational risks;
- minimization of risks related to personnel by means of establishing criteria on its' screening and examination, carrying out necessary events on personnel training.

The usage of the above methods leads to minimization of operational risks and allows to keep the loss from the operational risks occurrence at the level which does not influence the execution of Bank's obligations.

Internal procedures of estimation of capital adequacy ratio

The procedures of capital management of the Bank are in line with the requirements of the CBR reflected in the document dated 15 April 2015 № 3624-U *On the Requirements on Risk Management System and Capital Managemet* and also in line with the Component 2 of the Basel II document. They establish the following requirements for the Bank's own process of capital adequacy estimation:

- the existence of the corresponding corporate management tools;
- the existence of the organisational structure with the strict scope of duties;
- the existence of the sharp and effective system of the internal control.

The Bank on a regular basis develops a structured report (ICAAP) which comprises the basic features of the estimation of capital adequacy process, the susceptibility of the Bank to risks and the decision to be made on capital adequacy, considering the risks. The report also includes self-assessment of ICAAP, highlighting the directions for improvement, the drawbacks of the process, and aldo the corrective measures to be taken.

(Thousands of Russian Roubles)

26. Fair values of financial instruments

Fair value hierarchy

The Bank uses the following fair value hierarchy for measuring fair values of financial instruments:

- Level 1: quoted market prices (unadjusted) in an active market for an identical instrument;
- Level 2: valuation techniques for which all significant inputs are observable, either directly or indirectly;
- Level 3: valuation techniques which use significant unobservable inputs.

The table below analyses financial instruments measured at fair value at 31 December 2017, by the level in the fair value hierarchy into which the fair value measurement is categorised. The amounts are based on the values recognised in the consolidated statement of financial position:

	Level 1	*Level 2*	*Total*
Financial assets			
Available-for-sale securities	4 130 899	-	4 130 899
	4 130 899	**-**	**4 130 899**

The table below analyses financial instruments measured at fair value at 31 December 2016, by the level in the fair value hierarchy into which the fair value measurement is categorised. The amounts are based on the values recognised in the consolidated statement of financial position:

	Level 1	*Level 2*	*Total*
Financial assets			
Derivative financial assets	-	1 735	1 735
Available-for-sale securities	3 535 812	-	3 535 812
	3 535 812	**1 735**	**3 537 547**
Financial liabilities			
Derivative financial liabilities	-	786	786
	-	**786**	**786**

As at 31 December 2017, the Bank has repossessed collateral in the amount of RUB 194 854 thousand (2016: RUB 207 738 thousand) that is subsequently measured at lower of cost and fair value less cost to sell, for which fair value was determined using inputs that belong to Level 3 in the fair value hierarchy.

The estimation of fair value of repossessed collateral is based on the approaches depending on the type of repossessed collateral. These approaches are comparable, income approach and cost approach. The Bank adjusts the estimated market value of similar property using the liquidity discounts. The discounts, applied by the Bank ranges from 20% to 30% for residential property; 20% to 40% for office, trade, industrial and warehousing property, and 30% to 50% for cars and special vehicles, 40% to 50% for equipment.

Fair values of financial instruments carried at amortised cost

The estimated fair value of financial instruments carried at amortised cost as at 31 December 2017 and 31 December 2016 approximates their carrying values.

The estimates of fair value are intended to approximate the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants at the measurement date. However, given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realisable in an immediate sale of the assets or transfer of liabilities.

The objective of valuation techniques is to arrive at a fair value determination that reflects the price that would be received to sell the asset, or paid to transfer the liability in an orderly transaction between market participants at the measurement date. Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market-observable prices exist. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premia used in estimating discount rates.

(Thousands of Russian Roubles)

27. Related party transactions

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party directly, or indirectly through one or more intermediaries controls, is controlled by, or is under common control with, the entity; has an interest in the entity that gives it significant influence over the entity; the party is an associate of the entity; the party is a member of the key management personnel of the entity or its parent.

Banking transactions are entered into in the normal course of business with the Bank's shareholders and key management personnel. These transactions include loans, deposits and other transactions.

Since 2005 the Bank is a member of ISP Group. ISP Group members are entities comprising a banking group which has a leading position on the Italian market and a strong international presence, mainly in Central-Eastern Europe and the Mediterranean region.

Intesa Sanpaolo Holding International SA (Luxembourg) is a parent entity of the Bank as at 31 December 2017 owning 53.0228% of shares (2016: 53.0228%).

Intesa Sanpaolo S.p.A. (Italy) is the ultimate controlling party of the Bank as at 31 December 2017 and 2016. Transactions with foreign branches of Intesa Sanpaolo S.p.A. (Italy), which are located in different countries, are disclosed in the category named “Intesa Sanpaolo Group members”.

(Thousands of Russian Roubles)

The outstanding balances with the related parties as at 31 December are as follows:

	2017				**2016**			
	Intesa Sanpaolo S.p.A.	***Intesa Sanpaolo Holding International SA***	***Intesa Sanpaolo Group members***	***Key management personnel***	***Intesa Sanpaolo S.p.A.***	***Intesa Sanpaolo Holding International SA***	***Intesa Sanpaolo Group members***	***Key management personnel***
Cash and cash equivalents								
Current accounts and overnight placements with other credit institutions	749 346	-	298 800	-	792 933	-	1 020 979	-
Amounts due from credit institutions								
Time deposits	2 728 577	-	-	-	2 426 387	-	360	-
Loans to customers								
Loans to customers as at 1 January, gross	-	-	-	-	-	-	-	135
Loans issued during the year	-	-	-	18 861	-	-	-	-
Loans repaid during the year	-	-	-	-	-	-	-	(135)
Loans to customers as at 31 December, gross	-	-	-	18 861	-	-	-	-
Less: loan impairment allowance as at 31 December	-	-	-	(88)	-	-	-	-
Loans to customers as at 31 December, net	-	-	-	18 773	-	-	-	-
Amounts due to credit institutions								
Current accounts	945 357	-	19 097	-	2 083 577	-	4 726	-
Term deposits	-	-	-	-	1 276 222	-	-	-
Amounts due to customers								
Current accounts	-	-	-	11 268	-	-	-	12 968
Term deposits	-	-	-	38 790	-	-	-	22 130
Subordinated debt							-	-
Subordinated debt as at 1 January	-	-	2 426 712	-	-	-	2 915 308	-
Deposits received during the year	-	-	-	-	-	-	-	-
Deposits repaid during the year	-	-	-	-	-	-	-	-
Other movements	-	-	(121 873)	-	-	-	(488 596)	
Subordinated debt as at 31 December	-	-	2 304 839	-		-	2 426 712	-
Other liabilities	-	-	6 943	-	-	-	9 416	-
Derivative financial instruments	-	-	-	-	-	-	-	-
Notional amount of foreign exchange contracts	-	-	-	-	600 000	-	-	-
Derivative financial liabilities	-	-	-	-	(664)	-	-	-
Guarantees received by the Bank on loans and credit lines to customers	237 379	-	-	-	110 704	-	-	-

(Thousands of Russian Roubles)

The related profit or loss amounts of transactions with the related parties for the year ended 31 December are as follows:

	2017				2016			
	Intesa Sanpaolo S.p.A.	*Intesa Sanpaolo Holding International SA*	*Intesa Sanpaolo Group companies*	*Key management personnel*	*Intesa Sanpaolo S.p.A.*	*Intesa Sanpaolo Holding International SA*	*Intesa Sanpaolo Group companies*	*Key management personnel*
Interest income								
Amounts due from credit institutions	43 148	-	420	-	40 420	-	567	-
Loans to customers	-	-	-	1 017	-	-	-	3
Impairment of loans	-	-	-	(88)	-	-	-	2
Interest expense								
Amounts due to credit institutions	(12 019)	-	-	-	(7 895)	-	(214 882)	-
Amounts due to customers	-	-	-	(2 388)	-	-	-	(3 047)
Subordinated debt	-	-	(153 585)	-	-	-	(176 436)	-
Net (losses) gains from foreign currencies[1]	(36 600)	-	-	-	86 410	-	-	-
Fee and commission income	1 378	-	129 380	-	2 099	-	166 712	-
Fee and commission expense	(6 414)	-	(1 493)	-	(24 960)	-	(19 849)	-
Other general administrative expenses	-	-	(37 015)	-	-	-	(192 110)	-

Total remuneration of the Management Board members included in the personnel expenses for the year ended 31 December 2017 is RUB 78 315 thousand, including social contributions of RUB 7 017 thousand (2016: RUB 73 144 thousand, including social contributions of RUB 5 977 thousand).

Total remuneration of the Board of Directors for the year ended 31 December 2017 is RUB 18 862 thousand (2016: RUB 18 005 thousand).

As at 31 December 2017, the guarantees in the amount of RUB 246 310 thousand are represented by guarantees provided by ISP Group companies as counter-guarantees to the guarantees provided by the Bank (2016: RUB 237 228 thousand). The guarantees expiry dates vary from 31 January 2018 to 1 June 2019, commission rates vary from 0.15% to 0.4% (2016: expiry dates vary from 16 January 2017 to 30 November 2017, commission rates vary from 0.15% to 0.4).

The Bank counter-guaranteed RUB 256 528 thousand in relation to guarantees issued by ISP Group companies as at 31 December 2017, guarantees expiry dates vary from 15 March 2018 to 15 December 2018, commission rates vary from 1.0% to 2.0% (2016: RUB 68 565 thousand, guarantees expiry dates vary from 09 January 2017 to 15 March 2018, commission rates vary from 1.0% to 4.5%).

As at 31 December 2017 and 31 December 2016, guarantees received by the Bank on loans and credit lines have the same expiry dates as related loans. As at 31 December 2017 and 31 December 2016, the Bank didn't pay commission on these guarantees.

[1] Net gains from foreign currencies are calculated with marginal analysis

(Thousands of Russian Roubles)

28. Capital adequacy

The primary objectives of the Bank's capital management are the following:

- full compliance with the capital requirements imposed by the CBR and Russian legislation;
- maintaining the Bank's ability to continue as a going concern in order to maximize shareholder value and provide economic benefits to other parties;
- ensuring that the amount of capital is sufficient for business expansion and development.

The Bank monitors its capital adequacy using, among other measures, the ratios established by the Basel Capital Accord 1988, with subsequent amendments ("Basel Capital Accord"), and the ratios established by the CBR.

The Bank has complied with all externally imposed by the CBR capital requirements as at 31 December 2017 and 2016.

The Bank manages its capital structure and makes adjustments to reflect changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payments to the shareholders, return on capital to the shareholders or issue equity securities. No changes were made in the objectives, policies and processes from the previous year.

Capital adequacy under Russian Legislation

The Bank calculates amount of capital in accordance with Provision of the CBR dated 28 December 2012 No. 395-P *On Methodology of Calculation of Own Funds (Capital) of the Credit Organisations (Basel III).*

As at 31 December 2017, minimum levels of basic capital ratio (ratio N1.1), main capital ratio (ratio N1.2), own funds (capital) ratio (ratio N1.0) are 4.5%, 6.0% and 8.0%, accordingly (31 December 2016: 4.5%, 6.0% and 8.0%, accordingly).

As at 31 December 2017 and 2016, the Bank's CBR-defined capital adequacy ratios exceed the required statutory minimums and are as follows:

	31 December 2017	*31 December 2016*
Base capital	9 644 752	10 000 604
Additional capital	-	-
Main capital	**9 644 752**	**10 000 604**
Supplementary capital	2 735 855	2 712 747
Own funds (capital)	**12 380 607**	**12 713 351**
Risk-weighted assets (for basic and main capital ratios)	**62 119 235**	**63 054 879**
Risk-weighted assets (for own funds (capital) ratio)	**62 551 082**	**63 341 350**
Ratio N1.1 (%)	**15.5%**	**15.9%**
Ratio N1.2 (%)	**15.5%**	**15.9%**
Ratio N1.0 (%)	**19.8%**	**20.1%**

Capital adequacy ratio under the Basel Capital Accord (unaudited)

The Bank applies the Basel II Framework for the purpose of capital adequacy calculation using the simplified standardised approach for credit risk measurement, the standardised measurement method for market risk and the basic indicator approach for operational risk measurement. The Bank's capital adequacy ratio as computed in accordance with the Basel Capital Accord as at 31 December is as follows:

	2017	*2016*
Share capital	10 820 181	10 820 181
Retained earnings and other capital reserve	1 217 451	1 215 380
Deductions	(585 667)	(720 572)
Tier 1 capital	**11 451 965**	**11 314 989**
Revaluation of premises	384 144	-
Subordinated debt (unamortised portion)	2 304 839	2 426 712
Total capital	**14 140 948**	**13 741 701**
Risk-weighted assets	**75 764 158**	**65 002 924**
Tier 1 capital ratio	**15.1%**	**17.4%**
Total capital ratio	**18.7%**	**21.1%**

(Thousands of Russian Roubles)

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for unrecognised contractual commitments, with some adjustments to reflect the more contingent nature of the potential losses.

Gianluca Corrias	Chairman of the Management Board
Tatyana Pavlycheva	Member of the Management Board/Head of Accounting, Planning and Control Group/Chief accountant

19 February 2018