BANCA SISTEMA Group

DISCLOSURE BY INSTITUTIONS PURSUANT TO REGULATION (EU) NO. 575/2013 "THIRD PILLAR"

31 December 2020

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INTRODUCTION

With this document, the Banca Sistema Group (the "Bank" or "Banca Sistema") complies with the prudential supervisory provisions which, in order to strengthen market discipline, call for public disclosure obligations (the so-called third pillar) regarding:

- capital adequacy;
- risk exposure;
- the general characteristics of the systems in place to identify, measure and manage said risks.

The information subject to mandatory publication is of both a quantitative and a qualitative nature. It is divided into blocks ("sections"), and each of these addresses a specific disclosure area.

This public disclosure has been prepared in accordance with the following regulations:

- Regulation (EU) No. 575/2013 of 26 June 2013 (CRR) Part Eight "Disclosure by Institutions" (Articles 431 - 455) and Part Ten, Title I, Chapter 3, "Transitional Provisions for Disclosure of Own Funds" (Article 492);
- Directive 2013/36/EU (CRD IV); "Supervisory Provisions for Banks" - Bank of Italy, Circular No. 285 of 17 December 2013, as amended, implementing the provisions of the CRR and CRD IV;
- European Banking Authority (EBA) Guidelines EBA/GL/2014/14 - on materiality, proprietary and confidentiality and on disclosure frequency under Articles 432(1) and (2), and 433 of the CRR, and Guidelines EBA/GL/2016/11 - on disclosure requirements under Part Eight of Regulation (EU) No 575/2013;
- further EBA Guidelines regulating specific aspects of the Public Disclosure Requirements, including the Guidelines on Disclosure of Non-performing and Forborne Exposures (EBA/GL/2018/10).

Following the publication in the Journal of the European Union on 7 June 2019 of Regulation (EU) 2019/876 - also known as CRR II (Capital Requirements Regulation) - which is part of the broader regulatory reform package that also includes CRD V (Capital Requirements Directive), BRRD II (Banking Recovery and Resolution Directive) and SRMR II (Single Resolution Mechanism Regulation) - concerning disclosure requirements, in the fourth quarter of 2019 EBA prepared draft regulatory and implementing technical standards aimed at streamlining and standardising, consistent with the regulatory changes introduced by CRR II, which will apply starting in 2021, the periodic disclosure to be provided to the market. Specifically, EBA has submitted for public consultation:

- on 16 October 2019, the "Draft Implementing Technical Standards on public disclosures by institutions of the information referred to in Titles II and III of Part Eight of Regulation (EU) No 575/2013" document (EBA-CP-2019-09), which is designed to provide a single framework to harmonise market discipline under Article 434a "Uniform disclosure formats" of CRR II;
- on 22 November 2019, the "Draft Implementing Technical Standards on disclosure and reporting of MREL and TLAC" document, wherein the uniform disclosure formats and templates and related methodological instructions for using the templates are specified concerning the amount and composition of the "TLAC" (Total Loss Absorbing Capacity) standard introduced by CRR II and the "MREL" (Minimum Requirement for own funds and Eligible Liabilities) amended by BRRD II.

In the context of the COVID-19 pandemic, European and national Supervisory Authorities have issued measures and statutory requirements aimed at guiding the operations of banks with respect to supporting the real economy, clarifying certain interpretative aspects of prudential regulations and ensuring disclosure in the areas affected by the restrictive measures. The most significant regulations issued are outlined below:

- the EBA Guidelines on the treatment of legislative and non-legislative moratoria on loan repayments applied before 30 June 2020 (EBA/GL/2020/02), which specify that the moratorium alone does not represent a significant increase in credit risk. The EBA subsequently extended the regulatory treatment of both legislative and non-legislative moratoria until 30 September 2020;
- the Bank of Italy's communication issued at the end of March 2020 with a recommendation that no dividends be paid for the years 2019 and 2020 at least until 1 October 2020. This same communication contained the decision to allow banks to temporarily operate below the Pillar 2 Guidance (P2G), Capital Conservation Buffer (CCB) and Liquidity Coverage Ratio (LCR) requirements;
  - the EBA Guidelines (EBA/GL/2020/07) on reporting and disclosure of exposures subject to measures applied in response to the COVID-19 crisis, issued on 2 June 2020 and ratified by the Bank of Italy on 30 June 2020;
  - Regulation (EU) 2020/873 of 24 June 2020 (CRR "Quick fix") amending Regulations (EU) No 575/2013 and (EU) 2019/876 as regards certain adjustments in response to the COVID-19 pandemic;
- EBA Guidelines (EBA/GL/2020/12) of 11 August 2020 amending Guidelines EBA/GL/2018/01 on uniform disclosures under Article 473a of Regulation (EU) No 575/2013 (CRR) on the transitional period for mitigating the impact of the introduction of IFRS 9 on own funds

Reference context

Starting in March 2020, the Italian Government has introduced a series of measures intended to mitigate the economic effects associated with the spread of the COVID-19 pandemic by enacting several Law Decrees, including Law Decree no. 18 of 17 March 2020 (the "Cura Italia" Decree), Law Decree no. 23 of 8 April 2020 (the "Liquidity Decree"), Law Decree no. 34 of 19 May 2020 (the "Relaunch Decree") and Law Decree no. 104 of 14 August 2020 (the "August Decree"). Similarly, the Supervisory Authorities have enacted an extensive array of measures aimed at ensuring ample liquidity to all sectors of the economy, countering the risks of financial segmentation on a national basis, and ensuring the most effective transmission of monetary policy decisions. Within the above framework and with specific reference to credit risk are several measures such as the moratorium on credit and the introduction of public guarantees (SACE and the National Guarantee Fund) on new business loans. Among the measures introduced by the Supervisory Authorities are the European Banking Authority Guidelines on legislative and non-legislative moratoria on loan repayments applied in light of the COVID-19 crisis (EBA/GL/2020/02) transposed by the Bank of Italy in May 2020. These Guidelines specify the criteria for classifying a moratorium as a "general payment moratorium" and specify the correct prudential treatment of exposures subject to such legislative and non-legislative moratoria. To respond to the potential difficulties of customers arising from the temporary slowdown in the economic cycle and the possible effects on liquidity, the Banca Sistema Group has promptly implemented the above measures.

At 31 December 2020, the Banca Sistema Group comprised the Parent, Banca Sistema S.p.A., the subsidiaries ProntoPegno S.p.A., Largo Augusto Servizi e Sviluppo S.r.l., and Specialty Finance Trust Holdings Limited, a company incorporated under UK Law, and the Spanish joint venture EBNSistema Finance S.l.u.

On 24 June 2020, the Group received authorisation from the Bank of Italy to acquire the collateralised lending business unit of the Intesa Sanpaolo Group. The acquisition was completed on 10 July with effect from 13 July 2020.

At the end of 2020, Banca Sistema entered into an equal partnership with EBN Banco de Negocios S.A., taking a stake in the capital of EBNSISTEMA Finance S.L. to develop the Public Administration factoring business on the Iberian peninsula, specialising in the purchase of healthcare receivables.

Section	Description/CRR Reference/EBA Guidelines	Qualitative Disclosures	Quantitative Disclosures
1	Risk management objectives and policies (Art. 435)	x	N/A
2	Scope of application (Art. 436)	x	N/A
3	Own Funds (Art. 437)	x	x
4	Capital requirements (Art. 438)	x	x
5	Exposure to counterparty credit risk (Art. 439)	x	x
6	Capital buffers (Art. 440)	N/A	N/A
7	Indicators of global systemic importance (Art. 441)	N/A	N/A
8	Credit risk adjustments (Art. 442)	x	x
9	Unencumbered assets (Art. 443)	x	x
10	Use of ECAIs (Art. 444)	x	x
11	Exposure to market risk (Art. 445)	x	x
12	Operational risk (Art. 446)	x	x
13	Exposures in equities not included in the trading book (Art. 447)	x	x
14	Exposure to interest rate risk on positions not included in the trading book (Art. 448)	x	x
15	Exposure to securitisation positions (Art. 449)	x	N/A
16	Remuneration policy (Art. 450)	x	N/A
17	Leverage (Art. 451)	x	x
18	Use of the IRB Approach to credit risk (Art. 452)	N/A	N/A
19	Use of credit risk mitigation techniques (Art. 453)	x	x
20	Use of the Advanced Measurement Approaches to operational risk (Art. 454)	N/A	N/A
21	Use of Internal Market Risk Models (Art. 455)	N/A	N/A
22	Disclosure of Non-performing and Forborne Exposures (EBA/GL/2018/10)	x	x
23	Reporting and disclosure of exposures subject to measures applied in response to the COVID-19 crisis (EBA/GL/2020/07)	x	x

In this document, the disclosure required by sections: 6 “Capital buffers”, 7 “Indicators of global systemic importance”, 18 “Use of the IRB Approach to credit risk”, 20 “Use of the Advanced Measurement Approaches to operational risk”, and 21 “Use of Internal Market Risk Models”, is not provided herein, since it does not regard the scope of operations, the assumed risks, and the methods used.

Banca Sistema publishes this public disclosure and any subsequent updates on its Internet site at the address www.bancasistema.it, in the Pillar 3 section of the Investor Relations area.

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

QUALITATIVE DISCLOSURE

Risk culture

Banca Sistema ascribes great significance to risk management and control, as necessary conditions to guarantee the generation of sustainable value within a context of controlled risk.

Since 1 January 2014, the Bank has adopted an integrated reference framework both to identify its own risk appetite and for the internal process of determining capital adequacy. This system is the Risk Appetite Framework (RAF), designed to make sure that the growth and development aims of the Group are compatible with capital and financial solidity. The RAF comprises monitoring and alert mechanisms and related processes to take action in order to promptly intervene in the event of discrepancies with defined targets. The framework is subject to annual review based on the strategic guidelines and regulatory changes.

The risk management strategy seeks to acquire a complete and coherent vision of the Bank's risks by continuously stimulating the development of risk culture in all of the Bank's functions.

Consistent with the legal and regulatory provisions in force, the Bank adopts a three-level internal control system to monitor the risks it faces:

- **First level:** direct line controls to ensure the correct execution of the transactions, performed by the operational structures themselves (for example, hierarchical, systematic and test-checked controls), including by units dedicated exclusively to control duties that report to the managers of the operational structures – as far as possible – incorporated in IT procedures. These controls are carried out by the operational, business, and support functions (the "first level functions"). The operational structures bear primary responsibility for the risk management process.
- **Second level:** risk and compliance controls. Their purpose includes ensuring:
  - proper implementation of the risk management process;
  - observance of the operational limits assigned to the various functions;
  - the statutory and regulatory compliance of business operations, including self-regulation.

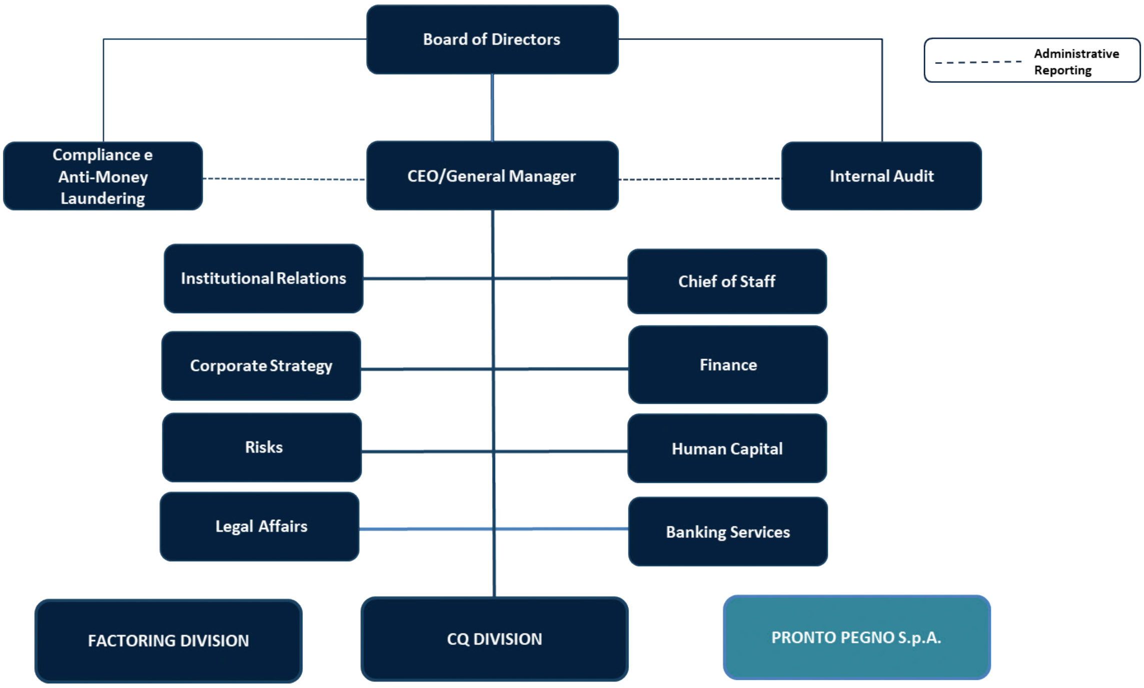
Second level controls are assigned to the Risk Department and the Compliance and Anti-Money Laundering Department.

- **Third level:** controls carried out through internal audits, focused on identifying the breaches of procedures and regulations, as well as on evaluating the completeness, adequacy, functionality, in terms of efficiency and effectiveness of the organisational structure of the other internal control system components and of the IT system (ICT audit), at regular intervals in relation to the nature and intensity of the risks. The third level controls are performed by the Internal Audit Department.

Organisational structure

A partire dal 1° febbraio 2020, la struttura organizzativa del Gruppo Banca Sistema è stata significativamente modificata, passando dal modello organizzativo funzionale ad un modello organizzativo di tipo divisionale; sono diventate pertanto operative due divisioni di business rispettivamente assegnate al presidio e allo sviluppo del Factoring e della CQ, Divisione Factoring e Divisione CQ, distinte dalle restanti Funzioni “centrali” (es. Internal Audit e Compliance & AML, Risk ecc. che, unitariamente, costituiscono il “Corporate Center”).

The organisational chart in force at 31 December 2020 is as follows:



The main roles and responsibilities of the corporate bodies/functions concerned in the overall risk management and control activity, as defined in the "General Bank Rules", are summarised as follows.

The corporate bodies, the internal governance structures and the departments responsible for ensuring the completeness, adequacy and reliability of the internal control system are:

Governance bodies

- The Board of Directors, which relies on the following internal Board Committees:
  - Internal Control and Risk Management Committee
  - Appointments Committee
  - Remuneration Committee
  - Ethics Committee
- The CEO/General Manager, who draws on the assistance of the following company committees:
  - Group Committee (Management Committee)
  - Risk and ALM Committee
  - Technical-Organisational Committee
  - Crisis Management Committee
  - CEO Credit Committee (only cases exceeding the authority of the division heads);
- **Control bodies**
  - Board of Statutory Auditors
  - Supervisory Body pursuant to Italian Legislative Decree no. 231/01
- **Company control functions**
  - Risk Department
  - Compliance and Anti-Money Laundering Department
  - Internal Audit Department
  - Manager in charge of financial reporting

Governance bodies: Board of Directors

The Board of Directors plays a central role both in the organisation of the Bank and in the management and coordination activities that the Bank exercises over the Banca Sistema Group, through strategic control over the development of the various business areas in which the Group operates and the risks identified in the activities carried out, management control aimed at ensuring the economic, financial and capital equilibrium is maintained by both the individual companies and the Group as a whole, and technical and operational control focused on assessing the various risk profiles attributed to the Group by the individual subsidiaries, as well as the Group's overall risks. To this end, the Bank's Board of Directors approves and periodically reviews the rules governing the management and coordination activities and verifies their proper implementation, promptly promoting any necessary corrective measures.

The Bank's Board of Directors is vested with all powers of ordinary and extraordinary management: it determines the overall governance structure of the Bank, establishes the strategic guidelines and objectives to be implemented by the Chief Executive Officer, oversees the system of controls necessary to monitor their implementation and performs the functions required under applicable legislation.

Internal board committees

To ensure an efficient system that provides the Board of Directors with an effective assessment of specific matters falling within its purview, Committees have been established that have been assigned powers and responsibilities with respect to various matters.

The Internal board Committees, established by the Board of Directors, are:

- Internal Control and Risk Management Committee;
- Appointments Committee;
- Remuneration Committee;
- Ethics Committee.

Internal Control and Risk Management Committee

The Internal Control and Risk Management Committee is made up of 4 non-executive and independent members and has the duty to assist the Board of Directors with preliminary advisory and proposal-making functions to conduct reviews and make decisions concerning the internal control and risk management system, including those affecting the periodic financial reports and those affecting risk management in response to problems brought to the attention of the Board of Directors.

Specifically, the Committee expresses its opinion to the Board of Directors in relation to the definition of the policies and the assessment, at least annually, of the adequacy of the control and risk management system, to the results presented by the Independent Auditor with regard to company accounting reports, evaluating the proper use of the accounting standards and their level of standardisation for the purpose of drafting the consolidated financial statements.

Appointments Committee

The Appointments Committee consists of three non-executive directors (at least two of which are independent) and plays an advisory and propositional role in identifying the best composition of the Board of Directors, indicating the professional figures whose presence may favour its proper and effective operation and, if necessary, helping prepare the Bank's Executive Directors succession plan. The Committee also plays an active role in appointing the managers of the company internal control functions. The Committee supports the process of appointing or co-opting directors and sets a target level for the less represented gender in order to ensure an adequate degree of diversification in the overall composition of the management body.

Remuneration Committee

The Remuneration Committee is comprised of three non-executive directors (two of which independent). It performs a proposal-making and investigation role vis-à-vis the Board of Directors, with regard to the definition of a remuneration policy for directors and key management personnel, including the remuneration for all of the key personnel as prescribed by Bank of Italy Circular no. 285/13. The Committee directly oversees the correct application of the rules concerning the remuneration of the managers of the company internal control functions, in accordance with the Board of Statutory Auditors.

Ethics Committee

The Ethics Committee is made up of three members, of which at least two meet the independence requirements. The office of Deputy Chairperson of the Bank's Board of Directors is an ex-officio member and is also the Chairperson of the Committee. The other two members of the Committee are chosen from among the non-executive directors of the Board of Directors. The Committee supports the Board of Directors in identifying and assessing the ethical principles for defining the conduct policy, evaluating the degree to which said principles must be applied to the corporate environment; it supervises over the publication of the Code of Ethics and the guidelines for external corporate communications regarding this matter.

Governance bodies: CEO and General Manager

The Chief Executive Officer is responsible for implementing the Bank's strategic and management guidelines, oversees implementation of the strategic guidelines, the RAF and the risk governance policies defined by the Board of Directors, and is responsible for taking all necessary steps to ensure that the organisation and the internal control system conform to the principles and requirements set out in Sections I and III of Bank of Italy Circular 285/2013, and monitors compliance with these principles and requirements on an ongoing basis.

Non-board committees

Group Committee (or Management Committee)

The Group Committee (or Management Committee), is a non-board committee, representing the unifying body within the Group's divisional organisational structure. It has the duty of assisting the Chief Executive Officer in implementing the governance, management and coordination policies approved by the Board of Directors on behalf of the Group members, resolving any critical issues and sharing information regarding the Bank in its entirety, the individual Divisions and the ProntoPegno subsidiary.

Its purpose is to share the decisions taken by the Chief Executive Officer, in exercising his/her delegated powers, with the Bank's senior management. The Group Committee is convened at least once a month by the Chief Executive Officer, who sets the agenda for the meetings and reports on any relevant issues that emerge or are discussed by the Committee to the Board of Directors.

Risk and ALM Committee

The Risk and ALM Committee supports the CEO in defining the strategies, the risk policies, and the revenue objectives, proposing interventions and strategies, for adapting thereto; it monitors capital adequacy with respect to the risk/profitability objectives, taking into account the various types of risks and the correlations between them. At the Risk and ALM Committee meetings, updates of the KRIs required under the RAF and the Recovery Plan are discussed, classifications of non-performing loans and any loans "returning to performing status" are assessed, the Impairment Document and the Credit Portfolio Report are discussed as are the assessments of the liquidity policies/Contingency Funding Plan (CFP) and their monitoring (Asset & Liability Management). More generally, all risk activities (IT risk, compliance risk, etc.) are monitored.

CEO Credit Committee

The CEO Credit Committee is a non-board committee that supports the CEO and Board of Directors in all decisions concerning credit transactions submitted that exceed the authority of the division heads or the CEO. It is chaired by the Head of Factoring Receivables in the capacity as Group Credit Supervisor. The Committee meets on an ad hoc basis and when there are specific business or organisational needs or requirements.

The CEO Credit Committee assesses and expresses a technical opinion on proposals concerning the granting and renewal of credit facilities.

Technical-Organisational Committee

The Technical-Organisational Committee supports the CEO in monitoring the organisation's technical and operational requirements, making proposals for intervention and improvement, and supervises over the setting up and development of the organisational model. It collects and examines the organisational proposals of the various functions, helping define corrective measures and coordinating new projects, defining their prioritisation and managing their implementation.

Crisis Management Committee

The Crisis Management Committee is the structure responsible for crisis management and, from its formation to its termination, it is the highest decision-making and governance body of the Bank during a crisis.

Control bodies: Board of Statutory Auditors

The Bank's Board of Statutory Auditors verifies that the Parent carries out its strategic and management control activities over the Group companies and works in close collaboration with the corresponding bodies of the subsidiaries.

The Board of Statutory Auditors is responsible for monitoring the completeness, adequacy, functionality, and reliability of the Internal Control System, the RAF and the ICLAAP process. It also supervises the observance of legal, regulatory, and statutory provisions, proper administration, the adequacy of the organisational and accounting structure, and the proper performance of the strategic and management control activities by the Bank.

When carrying out the necessary checks and inspections to fulfil this task, it calls upon the Bank's internal control structures and functions (Risks, Compliance and Internal Audit), from which it receives sufficient flows of information.

Supervisory Body pursuant to Italian Legislative Decree no. 231/2001

The Supervisory Body (or "SB") is a corporate body charged with overseeing the operation, effectiveness and application of the Organisational and Management Model (or "OMM") whose purpose is to prevent the offences specified in Italian Legislative Decree no. 231 of 8 June 2001. The SB also ensures that the OMM is continuously and promptly updated.

The SB is composed of 3 members appointed by the Board of Directors. The Chairperson of the Board of Statutory Auditors also chairs the SB; one member is chosen from independent directors and the third member is the Head of Internal Audit.

The SB's activities are governed by rules drawn up and approved by the SB itself.

Company control functions

The following organisational structures, which perform the activities prescribed for the company control functions, have been established within the Corporate Centre of Banca Sistema:

- The Risk Department reports directly to the CEO. It is tasked with the identification, management and monitoring of all risks to which the Bank is or may be exposed. The Risk Department collaborates in the formulation and implementation of the Risk Appetite Framework (RAF) and the related risk governance policies, and the various stages that make up the risk management process as well as in setting operational limits for the assumption of various types of risk.
- The **Compliance and Anti-Money Laundering Department**, which reports to the Board of Directors and is managed by the Chief Executive Officer, is responsible for managing compliance risk with regard to all the business activities, verifying that the internal procedures are suitable to prevent said risk. The Department collaborates with other departments of the Bank for the definition of methods for the assessment of compliance risks. This Department includes the Anti-Money Laundering Department, which is responsible for performing audits on the application of relevant laws and regulations using a risk-based approach.
- The **Internal Audit Department** reports directly to the Board of Directors and is managed by the CEO. The Internal Audit Department performs third level assessments of the overall functioning of the internal control system, bringing possible improvements to the attention of the Corporate bodies. In particular, the Department assesses the completeness, adequacy, functioning, and reliability of the components of the internal control system, of the risk management process, and of the company processes, also having regard to the capacity to identify errors and irregularities. In this context, among other things, it inspects the company risk control and compliance departments. The Head of the Internal Audit Department is also the delegated officer pursuant to Article 36 of Italian Legislative Decree No. 231/07 as well as the Data Protection Officer of Banca Sistema, in accordance with Regulation (EU) No. 679/2016.
- The **Manager in charge of financial reporting** sets policies, coordinates administration, and monitors the accounting and financial reporting internal control system within the Group. The Manager in charge of financial reporting also supervises the implementation of compliance measures according to the generally applicable rules of the Bank, as approved by the Board of Directors. The Manager in charge of financial reporting also receives the reporting package of the ProntoPegno S.p.A. subsidiary, as approved by the Board of Directors, and uses it to prepare the Group's consolidated financial statements.

The aforementioned Departments/Functions are organisationally separate from each other. Internal regulation defines the roles, responsibilities, tasks, operating procedures, reporting flows and planning of control activity at the corporate level.

In detail:

- Each year, the Risk Department and the Compliance and Anti-Money Laundering Department present the corporate bodies, each based on their respective areas of competence, an activity schedule that identifies and assesses the main risks to which the Bank is exposed and the relevant management measures. The intervention scheduling takes into account both any deficiencies observed in the inspections, and any new risks identified.
- Each year, the Internal Audit Department presents the corporate bodies an audit plan that indicates the scheduled auditing activities, taking into account the risks of the various activities and company structures. The plan contains a

specific section relative to the auditing activity on the IT system (ICT auditing).

At the end of the management cycle, hence annually, said departments present the corporate bodies a report on the activities carried out, illustrating the audits performed, the results obtained, any weaknesses observed, and they propose interventions to be adopted to eliminate them; furthermore, each for the aspects relevant to their corresponding remit, they report on the completeness, adequacy, functionality, and reliability of the internal control system.

Disclosure of the governance system (Art. 435(2) CRR):

Pursuant to the Bank's Articles of Association, the Board of Directors can be composed of a minimum of 7 and a maximum of 11 members who:

- bring to the company the specific skills they possess;
- are aware of the tasks and responsibilities of their role and are in possession of the requirements set forth by law and regulations in force at the time;
- act and resolve with full knowledge of the facts and autonomously in pursuit of the aim of creating value for shareholders;
- only accept the position when they believe they are able to dedicate the time needed to diligently carry out their tasks, also being mindful of the number of positions of director or statutory auditor they have in other companies or bodies;
- keep the information acquired as a result of the office held as confidential.

The members of the management body shall remain in office for three financial years (their office shall end on the date of the Shareholders' Meeting called to approve the financial statements for the last year of their office) or for any shorter period which may be established by the Shareholders' Meeting at the time of appointment. Directors may be re-elected.

Pursuant to article 10.3 of the Articles of Association, the directors must meet the requirements of professionalism and integrity and any other requirement under the regulations in force and the Articles of Association.

The current members of the Board of Directors are listed below:

Chairperson	Ms. Luitgard Spögler[1]
Deputy Chairperson	Mr. Giovanni Puglisi *(Independent)*
CEO and General Manager	Mr. Gianluca Garbi
Directors	Mr. Daniele Pittatore *(Independent)* Ms. Carlotta De Franceschi *(Independent)* Ms. Laura Ciambellotti *(Independent)* Mr. Federico Ferro Luzzi *(Independent)* Mr. Francesco Galietti *(Independent)* Mr. Marco Giovannini *(Independent)*

(1) Meets the independence requirement pursuant to art. 147-ter, paragraph 4, and art. 148, paragraph 3 of Legislative Decree no. 58 of 24 February 1998, but it also does not meet the provisions of art. 3, application criteria 3.c.1.b and 3.c.2 of the Code of Conduct issued by Borsa Italiana.

The following table summarises the number of positions held in other companies by members of the Board of Directors as at 31 December 2020:

Directors	Total number of positions held in other companies
Luitgard Spögler	1 (non-executive)
Giovanni Puglisi	0 (non-executive)
Gianluca Garbi	0 (non-executive)
Laura Ciambellotti	0 (non-executive)
Daniele Pittatore	2 (non-executive)
Carlotta De Franceschi	2 (non-executive)
Francesco Galietti	0 (non-executive)
Marco Giovannini	2 (executive)
Ferro Luzzi	2 (non-executive)

Risk management and hedging policies

Based on the analysis conducted, the Bank, considering its current and future operations, is exposed to the following risks at 31 December 2020:

Pillar 1 risks: typical banking risks, such as credit risk (which also includes counterparty risk), market risk and operational risk. Following the introduction of the rules on liquidity risk management, short-term liquidity risk (Liquidity Coverage Ratio - LCR) and long-term liquidity risk (Net Stable Funding Ratio - NSFR) are also included.

Pillar 2 risks include:

- concentration risk;
- liquidity risk;
- excessive leverage risk;
- interest rate risk on the banking book;
- strategic risk;
- reputational risk;
- compliance risk.

Other Risks: these include country risk and Italy sovereign risk.

The Bank instead is not exposed to residual risks, participation risk, basis risk, transfer risk, or securitisation risk.

To determine the prudential capital requirement on Pillar 1 and 2 risks, the Bank uses standard methods, which will be more clearly described in the following paragraphs.

Pillar I

Credit risk consists of the risk that the counterparty is unable to honour its contractual commitments, thus resulting in an unexpected loss thereto so as to place its financial stability at risk in the immediate future.

This is the biggest risk facing the Bank, covering about 74% of the allocated internal capital.

The principal types of Bank operations that originate credit risk are listed as follows:

- acquisition of receivables with and without recourse (factoring);
- purchases of loans granted in the form of salary- and pension-backed loans from other intermediaries;
- direct granting of loans in the form of salary- and pension-backed loans;
- loans to small and medium-sized enterprises, covered by the National Guarantee Fund;
- collateralised lending (mainly secured by gold);
- medium-term corporate loans (with guarantee from SACE or the National Guarantee Fund - FNG);
- financial instruments held on its own account;
- loans to supervised brokers.

The core business of the Bank is represented by its factoring activity (especially with the Public Administrations), which features its own peculiar types of risk. This activity relies on a more complex evaluation process (debtors, assignors, and supply contract) and benefits from revolving credit.

Factoring activities make effective risk mitigation possible, through reviews of the financed transaction and observation of the assigned debtors' payment patterns.

The credit risks from factoring activities also include:

- "dilution risk", i.e. the possibility that the purchased loan or receivable is no longer fully enforceable at the due date due to offsets, abatements, disputes between the assigned debtor and the assignor. The Bank has obtained appropriate protection against this risk by implementing specific contractual clauses;
- "claw-back" risk: pursuant to Law 52/1991, when the assignment of a receivable is notified to the assigned debtor, the latter is still obligated to pay the factor for the amounts of the loan/receivable covered by the assignment agreement, even if the assignor goes bankrupt. The receiver bears the burden of proving that the factor was aware of the state of insolvency. If the receiver were to prove that the assignee was aware of the assignor's insolvency at the time of the assignment, the assignment itself would cease to be enforceable, and the payments received from the assigned debtor would have to be returned to the receiver.

Credit process and involvement of the control functions

The credit risk management process provides for the involvement of the various internal functions of each division. This organisation of activities allows, via the specialisation of the resources, a high degree of efficiency and standardisation in overseeing credit risk and monitoring individual positions.

In each Division, the credit risk generation process (the lending process) is broken down into different phases, which are summarised as follows:

- Commercial contact and preliminary activities: contact with potential customer and document gathering;
- Credit review process: analysis and assessment of the creditworthiness of the customer, the assigned debtor and the underlying asset;
- Decision and related activities: approval by the decision-making body on the factoring transaction agreed with the customer and commencement of activities to complete the transaction;
- Requests for insurance policies from the company: only valid for salary- and pension-backed loans;
- Execution and completion: execution of the agreement and completion of the transaction;
- Payment and management of collections: financing of the transaction and management of collections on the purchased receivable;

- Monitoring: continuous monitoring of the position for the management of any actions to be taken in the event of default (possible judicial recovery). In this regard, within the two Divisions, the Group has set up the Credit Monitoring and Reporting Function which monitors and supervises the Factoring product portfolios, and the Credit and After-Sales CQ Function which manages the part relating to the salary- and pension-backed loan portfolio.

The Risk Department participates in the credit review activities of compliance with the Key Risk Indicators (KRI) for Large exposures and in issuing opinions on compliance with the RAF in the event of More Significant Transactions (MST), while the Anti-Money Laundering and Compliance Department participates through monitoring customer due diligence.

The Credit Department of the relevant Division is responsible for proposing the classification of the default positions. Based on the assessments made, it proposes the appropriate classification of exposures to be submitted to the CEO for a decision. The CEO shall assess the change in status after receiving the opinion of the Risk and ALM Committee.

Finally, the Internal Audit Department performs a specific annual audit of the entire factoring process.

The credit risk management and mitigation controls specifically implemented to address the various transaction types are briefly discussed below.

a. **Acquisition of receivables with and without recourse (factoring):** Banca Sistema's policy predominantly consists in the purchase without recourse of business receivables owed by central administrations, territorial bodies, and, in general, by the Public Administration, and is characterised by the direct assumption of final debtor's credit risk. Credit risk is generated by a direct result of the definitive acquisition of credit from the customer company versus the insolvency of the assigned debtor.

b. **Salary- and Pension-Backed Loans (indirect channel):** Beginning in June 2014, Banca Sistema ("Assignee") extended its own business to the purchase without recourse, from financial companies operating in this sector ("Assignor"), of receivables resulting from loans payable through:
   - salary-backed loans to employees in the public and private sector;
   - pension-backed loans;
   - salary deductions to public sector employees.

c. **Salary- and Pension-Backed Loans (direct channel):** Following the merger of Atlantide S.p.A., the Banca Sistema Group has expanded its retail offering with the direct origination of salary- and pension-backed loans through a new product, QuintoPuoi. QuintoPuoi is distributed through a network of single-company agents and specialised brokers located throughout Italy.

   The Bank has started an un-brokered direct origination activity whereby bank employees telephone customers who may be interested in taking out a loan. These customers make their intentions known through specific internet searches which are collected and reported by specialist operators (leads) or by applying directly through the bank's portal. They are then contacted by telephone by a bank employee who offers them the possibility of taking out a loan. The activities tied to finalising the loan can be carried out at a bank branch, through the agency network or using an electronic signature.

   The Bank recognises the life insurance policies taken out in favour of the lending institution as a means of reducing the credit risk (after the assignment, the Bank becomes the beneficiary of the policies), provided that those policies meet the conditions specifically indicated in Regulation (EU) 575/13, Art. 212, paragraph 2 – Requirements for other funded credit protection.

d. **Loans contingent on issuance of guarantee by the National Guarantee Fund for SMEs:** Loan made by Banca Sistema to firms classified as micro, small and medium enterprises (SMEs). The granting of a loan is contingent upon the presence of the guarantee issued by the National Guarantee Fund (Fund) for SMEs (Italian Law no. 662/96 as amended) managed by Mediocredito Centrale S.p.A. (MCC).

   The presence of the Fund guarantee strictly limits the Bank's credit risk to the unsecured portion of the loan.

Beginning in 2017, the Bank decided to halt development of this business line after regulatory changes affecting the SME Loans product with MCC guarantee, for which the guaranteed percentage will be reduced. Therefore, it is no longer deemed profitable by the Bank.

e. **Collateralised loans:** Beginning in 2016, Banca Sistema extended its own business to opening credit lines on a current account secured by collateral. The loan is generally granted in exchange for an asset that is pledged as collateral (in the form of gold) that mitigates the risk. The duration of the loan varies from three to twelve months and may be renewed for a maximum of three years. On 1 August 2019, ProntoPegno S.p.A., a company wholly owned by the Parent Banca Sistema focused on collateralised lending, began operating. On 24 June 2020, the Group received authorisation from the Bank of Italy to acquire the collateralised lending business unit of the Intesa Sanpaolo Group. The acquisition was completed on 10 July with effect from 13 July 2020.

f. **Medium-term corporate loans (with guarantee from SACE or the National Guarantee Fund - FNG):** In response to the spread of the Coronavirus, starting in the third quarter of 2020, the Bank granted loans to businesses with a duration of no more than 6 years (including the possibility of deferring the repayment of the principal for up to 24 months). These loans are guaranteed either by the National Guarantee Fund for SMEs or by SACE.

g. **Financial instruments held on its own account:** Investments in Italian government securities for which the Bank has set up a specific system of limits, structured so as to guarantee a careful and balanced management of operational autonomies within the scope, among other things, of the transactions regarding financial instruments recorded in the banking book and held on its own account, are classified in this portfolio. Italian government security trading operations entail a credit risk exposure to central administrations.

h. **Loans to supervised brokers:** Any excess liquidity is for the most part placed in the interbank market, resulting in a credit risk exposure to supervised brokers. "Hot money" transactions, i.e. short-term loans to primary financial institutions also generate exposures to supervised brokers.

With regard to protecting against credit risk, in 2020, the Risk Department of the Parent, along with the well-established second level controls and the periodic monitoring, was involved in a special project regarding the application of the new definition of default starting on 1 January 2021.

Always with respect to credit risk controls, the Bank, following the divisionalisation process, has set up separate Credit Committees for the two Factoring and CQ Divisions, within which decisions may be taken up to pre-defined credit mandates, while a CEO Credit Committee has been set up for transactions that exceed the powers of the individual Divisions. At the same time, the Credit Coordination Committee was introduced, which makes it possible to ensure consistency in the granting of credit and close monitoring of individual positions.

For the purpose of determining the internal capital with respect to credit risk, the Bank uses the standardised approach, provided for the determination of the regulatory requirements with respect to credit risk.

The internal capital with respect to credit risk is, therefore, equal to the capital requirements defined in accordance with Pillar 1 regulations. The capital requirement is constantly measured and reported quarterly to the Bank of Italy.

In general, continuous analyses and measurements aimed at classifying exposures among the credit quality risk categories are conducted for all credit risk exposures, where deemed expedient.

Counterparty risk is the risk that the counterparty of a transaction having as its subject matter specific financial instruments may be in default prior to the settlement of the transaction itself[2]. It differs from credit risk by virtue of the type of transactions to which it refers; typically, these can be attributed to transactions that generate an exposure equal to their positive fair value, that have a market value evolving over time based on underlying variables and generate an exchange of payments, financial instruments or commodities against payments. A distinctive feature of counterparty risk consists in determining a bilateral-type risk, for which both counterparties are exposed to the risk of incurring unforeseeable losses.

In relation to Banca Sistema's operations, the risk is generated mainly by repos having as the counterparty the Compensation and Guarantee Fund or other institutional counterparties. The comprehensive method is used to measure counterparty risk[3].

Market Risk consists in the downside risk to which a financial intermediary is exposed from conducting financial instrument trading transactions in markets. In particular, the risk of posting losses due to adverse trends in the reference market, that could cause an unexpected and unforeseeable reduction in the value of the instruments held.

These are risks generated by market trading transactions regarding financial instruments and currencies which are relevant to the following components:

- position risk, divided into generic risk, caused by an unfavourable price trend of the bulk of the instruments traded, and specific risk, due to factors related to the issuer's status;
- settlement risk, including the transactions not yet settled after the due date that expose the Bank to the downside risk deriving from non-settlement of the transaction;
- concentration risk, which calls for a capital requirement specific for the banks that, as an effect of the risk positions relative to the regulatory trading book, exceed the individual credit line limits;
- foreign exchange risk, which is the risk of incurring losses as a result of adverse changes in the prices of foreign currencies.

The internal capital with respect to market risk is determined in accordance with the standardised approach. This approach envisages the calculation of the requirement based on the so-called “building block approach”, according to which the overall requirement is given by the sum of the capital requirements determined for the individual market risks (position, settlement and concentration risk). This approach is prudential: by linearly summing the individual requirements, the benefits provided by diversification are ignored, thus obtaining a capital requirement greater than the risk assumed.

The Risk Department prepares specific reports for the Risk and ALM Committee, the CEO, and the Board of Directors.

As at 31 December 2020, the Bank was not exposed to market risk.

(2) See “Supervisory provisions for banks” – Bank of Italy, Circular no. 285 of 17 December 2013, Part II, Chapter 7, as amended.

(3) See Regulation (EU) 575/2013 Title II, Chapter 4.

Operational Risk is the risk of loss arising from inadequate or non-functioning internal processes, human resources or systems, or from external events.

In this context, the Bank implemented an operational risk management process (Operational Risk Framework) to identify, measure, and monitor the operational risk.

The information and communication technology (ICT) risk is the risk of incurring economic, reputational and market losses in relation to the use of information and communication technology. In the supplemented representation of the business risks, this type of risk is considered – in accordance with the specific aspects – among operational, reputational and strategic risks.

The Bank continuously monitors the ICT risks based on the continuous information flows between the functions affected by the ICT risk assessment, assuring consistency between the results deriving from the ICT risk assessment and what has emerged in the operational risk assessment.

As an additional protection against operational risk, the Bank:

- has stipulated an insurance policy on operational risks deriving from actions of third parties or caused to third parties, as well as suitable riders to cover the damages caused by suppliers of infrastructures and services, and it approved a Business Continuity Plan. Moreover, effective 31 December 2019, the Bank entered into a cyber risk policy to mitigate the impact stemming from possible cyber attacks for unauthorised access to corporate systems;
- has strengthened its security infrastructure by implementing security measures to increase the level of security for remote activities;
- has introduced tools to counter cyber attacks via e-mail (phishing).

Basel III Ratios- Liquidity Coverage Ratio and Net Stable Funding Ratio: The LCR is a regulatory liquidity ratio that measures the short-term (30-day) liquidity position and is calculated as the ratio between the stock of High-Quality Liquid Assets (HQLA) and the net outflows over a 30-day period.

The monitoring of this ratio makes it possible to verify whether the Bank maintains a level of high-quality liquid non-term restricted assets, readily convertible into liquidity to satisfy the needs relative to a time interval of 30 days, during any particularly significant liquidity stress scenario. The stock of liquid assets should at least allow the Bank to honour its financial commitments over a time horizon of thirty days, a period within which it is supposed appropriate remedial actions on the part of the corporate bodies and/or by the Supervisory Authorities may be taken in order to rectify any deficit observed.

With regard thereto, Banca Sistema, prudentially, during 2020 constantly maintained a large quantity of securities and readily liquid assets hedging potential outflows of liquidity.

The Bank specifically monitors the short term Liquid Coverage Ratio (LCR) defined by the ratio between the stock of high-quality liquid assets (HQLA) and the net outflows over a time horizon of 30 days.

With reference to the structural liquidity ratio, the Bank uses the Net Stable Funding Ratio (NSFR) defined by the ratio between the available amount of stable funding and the required amount of stable funding. This ratio establishes a minimum acceptable amount of stable funding based on the liquidity characteristic of the assets and on the transactions of an institution over a time horizon of one year. Use of the NSFR should prevent an excessive recourse to short-term wholesale funding on the part of the Bank.

Pillar 2

The Bank is exposed to the following Pillar 2 risks.

The relevant legislation with regard to prudential supervision (Bank of Italy Circular 285/13, as amended) defines **Concentration Risk** as the risk deriving from exposures to counterparties, groups of associated counterparties and counterparties of the same economic sector or that carry out the same activities or are in the same geographical segment.

The Bank measures geo-sectoral concentration risk following the proposed ABI approach. This allows the effects on the internal capital caused by changes of sectoral concentration to be assessed. Said effects are calculated using a benchmark with respect to which, by applying a mark-up coefficient, any adjustment of internal capital (Add-on) is quantified.

Furthermore, the bank measures the single-name concentration risk using the standard approach indicated by the Supervisory Authority[4]. This method triggers a capital add-on according to the Herfindahl index, which is calculated according to exposures, and a proportionality constant, calibrated according to the riskiness of the portfolio.

Interest Rate Risk represents the risk, current or prospective, of a decrease of value of the capital or a decrease of the net interest income deriving from the impacts of the adverse changes in the interest rate.

The exposure to interest rate risk on the banking book is calculated as provided for by current regulations, via the simplified regulatory approach[5].

In light of the proposed amendments to Circular 285/2013, the Risk Department has updated the simplified calculation approach based on the new regulatory provisions.

In this way, the Bank is able to monitor the impact of unexpected changes in market conditions on equity, thus identifying the relative mitigation measures to be implemented.

The company departments responsible for guaranteeing the correct management of the interest rate risk are the Treasury Department and the Risk Department, which are responsible for determining the most appropriate risk indicators and for monitoring the performance of the assets and liabilities, and management, which has the specific duty of annually presenting the Board of Directors with investment, funding, and interest rate risk management policies, as well as suggesting during the year any expedient interventions to ensure the performance of the activity consistent with the approved risk policies.

As at 31 December 2020, no interest rate risk hedging instruments were used.

Liquidity Risk is defined as a form of default on the payment commitments and may be caused by:

- Funding Liquidity Risk: the inability to acquire funds or to honour one’s own payment commitments at market cost, i.e. incurring high funding costs.
- Market Liquidity Risk: presence of limits to the sale of assets or of losses on the sale of the said assets.

In detail, the following distinctions can be made concerning liquidity risk:

- Mismatch liquidity risk: the risk deriving from the asymmetry between the amounts and/or the maturities of the incoming and outgoing flows deriving from the Bank's operations, with reference both to the contractual maturities and conduct.
- Contingency Liquidity Risk: the risk deriving from unexpected future events that may require an amount of liquidity greater

(4) See "Supervisory provisions for banks" - Bank of Italy, Circular no. 285 of 17 December 2013 as amended, Part One - Title III, Chapter 1, Schedule B.

(5) See Circular no. 285/2013, Part One, Title III, Chapter 1, Schedule C.

than that currently considered to be necessary; it is the risk of not honouring sudden and unexpected short-term payments.

The method used by the Bank to measure liquidity risk is based on the liquidity gap approach indicated in the Bank of Italy guidelines.

Also in regard to the liquidity KRIs, the Bank constantly monitors the level of **Readily Monetizable Assets**, i.e. the level of securities issued by Member States in the EMU that are denominated in Euro, not structured, and accepted as collateral for refinancing operations at the ECB, and by cash.

Furthermore, to guarantee an adequate level of protection against liquidity risk, the provisions issued by the Basel Committee in terms of the matters below were applied:

- the formalisation of liquidity risk governance policies, consistent with the characteristics and the size of the transactions;
- the assessment of net financial position;
- the performance of periodic stress tests (sensitivity analysis for class 3 Banks) to evaluate the impact of negative events on risk exposure and on the adequacy of the liquidity reserves;
- the constant retention of adequate liquidity reserves;
- the definition of operational limits;
- the definition of appropriate liquidity risk mitigation instruments, first by drafting an adequate Contingency Funding Plan, that guarantees the protection of capital in situations of liquidity drainage, via the preparation of crisis management strategies and procedures for acquiring funding sources in case of emergency.

In order to determine an adequate protection against Liquidity Risk, roles and responsibilities were identified, in particular:

- Treasury Department (first level protection) which represents the first line of protection in managing liquidity risk. The department calculates and monitors the risk indicators;
- Every month, the Risk Department (second level protection) conducts the second level controls in liquidity risk management and continuously assesses the adequacy and proper implementation of the Liquidity Policy and of the Contingency Funding Plan.

The liquidity situation is subject to careful, continuous monitoring by the Treasury Department and the Risk Department, inter alia at the Risk and ALM Committee meetings.

The Risk Department periodically submits reports on liquidity risk to the CEO and the Board of Directors.

Through the Liquidity Policy and the Contingency Funding Plan, the Bank has structured the liquidity management on three interconnected levels, which correspond to specific purposes:

- **Operational liquidity** (short term – up to 12 months), with the purposes of guaranteeing the Bank's capacity to honour its anticipated and unforeseen cash payment commitments for the next 12 months;
- **Structural liquidity** (medium/long term – beyond 12 months), meant to maintain an adequate ratio between overall liabilities and medium/long-term assets aimed at avoiding pressure on current and prospective sources in the short term;
- **Contingency Funding Plan** (CFP), which regulates the process, the roles and the responsibilities in case of liquidity crisis situations.

The liquidity management policy and the CFP provide for the following fundamentals:

- identifying tasks and responsibilities to be assigned to the company departments involved in the liquidity management process;

- defining the operating processes associated with the activities to be carried out;
- determining the measurement tools;
- defining the Operational Limits, Warning Indicators, and Tolerance Thresholds.

Risk of Excessive Leverage means the risk that a level of debt particularly high with respect to the bank's own funds renders the Bank vulnerable, and corrective measures have to be adopted in its Business Plan, including distressed selling of assets which might result in losses or in impairment losses on its remaining assets.

The indicator is reported quarterly to the Bank of Italy for monitoring purposes. Throughout 2020, Banca Sistema has always maintained an indicator level above the regulatory limit proposed by the Basel Committee.

To forestall that risk, the Bank, acting in accordance with Regulation (EU) no. 575/2013 and Bank of Italy Circular no. 285/2013, calculates the Leverage Ratio by using the method provided in that Regulation. The Leverage Ratio is calculated as the ratio between Tier 1 Capital and Total Adjusted Assets, and is monitored within the Risk Appetite Framework of the Bank.

Reputational Risk is the risk of incurring losses subsequent to events capable of worsening the image of the bank in the eyes of the various types of stakeholders (shareholders, customers, counterparties, investors, Supervisory Authorities). Said negative perception may be due as much to direct experiences of the considered parties, as to sensations thereof, not necessarily caused by concretely observable events.

Reputation is associated with the sum of factors whose value expresses the company's capacity to create "wealth" not only for its shareholders but, in a more extensive sense, for all the stakeholders.

Knowledge of the difficulties associated with quantifying reputational risks have driven the Bank to implement suitable measures to mitigate them, focusing its inquiries on the quality of the organisational and control structures.

Within this framework, the utmost consideration was given to profiles capable of guaranteeing substantial compliance with the correctness and professional competence requirements, with particular regard to:

- the level of awareness of the top management bodies regarding the relevance of this aspect;
- the promotion of a culture of ethics and correct conduct at all levels of the company;
- the suitable management of relations with all stakeholders;
- the suitability of the risk management and mitigation systems;
- the effectiveness of controlling action by the Supervisory Body.

Strategic Risk is the risk, current or prospective, of a decrease in earnings or capital, which can generally be attributed to four very specific cases:

- changes in the business environment;
- erroneous company decisions;
- inadequate implementation of decisions made;
- poor or erroneous reactivity to changes in the business environment (structural break).

The onset of strategic risk, therefore, can be attributed to a situation of discontinuity in the normal performance of business activities, whether due to internal or external changes to the company scope. Conversely, the risk in question may be considered substantially non-existent in the presence of presumable stability of the normal course of business management.

It would be advisable to place special emphasis on the fact that, as it is configured, this risk takes on a connotation of peculiar criticality, due to the elevated dynamism required by the decision-making bodies in defining adequate and prompt corrections consistent with the continuous changes in the macroeconomic context/business cycle characterising the market in which the Bank operates.

A few cases that may typically lead to strategic risk are listed below:
- acquisition transactions/partnerships;
- changes in the company structure;
- consolidation operations/growth in size meant to attain economies of scale;
- diversification of products and distribution channels;
- technological innovation and operational optimisation oriented towards increasing the quality of the services offered.

Compliance Risk is the risk of non-compliance with laws and regulations and of incurring judicial or administrative penalties, significant financial losses or damages to reputation as a consequence of violations of mandatory provisions (as prescribed by law or regulations) or also of self-regulation (for example articles of association, codes of conduct, corporate governance codes).

This risk affects all levels of the corporate structure, especially in connection with the operating lines. Prevention has to start where the risk is generated. Therefore, all personnel must be made adequately responsible for their actions.

Generally, the most significant regulations for the purpose of compliance risk are those regarding the performance of intermediation activity, the regulations to prevent money laundering, the management of conflicts of interest, the transparency with respect to customers and, more generally, consumer protection laws.

Risk mitigation is pursued by a careful management of the operational autonomy, establishing limits in terms of both responsibility and consistency and composition of the portfolio by type of securities.

The Bank is evaluating the possibility of also monitoring conduct risk. This risk is defined as the actual or prospective risk of loss resulting from an inappropriate offer of financial services and the resulting legal costs, including cases where conduct is intentionally improper or careless.

Other Risks

Country Risk represents the risk of losses caused by events occurring in a country other than Italy. The concept of country risk is broader than that of sovereign risk as it relates to all exposures regardless of the type of counterparty, be it an individual, a company, a bank, or public administration.

In general, country risk stems from the possibility of loss due to events that are not dependent on the solvency of the debtor, but are attributable to the country, considered in a broad sense, in which the debtor resides. Any international loan involves country risk because the debtor's ability and/or possibility of repaying the loan may be affected by economic, political, and social factors that go beyond the microeconomic aspects of the credit relationship. If the debtor is a private party, this risk takes the form of a series of political, economic and/or technical impediments for which the public authority is ultimately responsible. If, on the other hand, the debtor is the government of a country or any other public or publicly guaranteed entity (a sovereign debtor), this risk manifests itself in the direct inability (technical, economic, financial) or refusal of these entities to honour their commitments.

Italy's Sovereign Risk represents the risk that the Italian government will default on its financial obligations due to economic, financial, and political factors.

Reporting system

The Risk Department constantly informs the management bodies on the level of risk assumed by the Bank through a reporting system that follows a specific frequency according to the contents.

All the analyses performed by the Risk Department on the observed potential risk areas and on possible mitigation measures are formalised in the quarterly Tableau de Bord or on other specific analysis documents submitted to the attention of the Risk and ALM Committee, of the Internal Control and Risk Management Committee, and of the Board of Directors, together with the Board of Statutory Auditors.

Reporting/control	Description	Recipient	Frequency
Monitoring loans and receivables portfolio	Analysis of contingent risks of every portfolio to be purchased (e.g. Large Exposures, MST, etc.)	Risk Department	By event
Treasury position	Review of compliance with treasury powers delegated to the CEO	Risk Department	Daily
Credit Risk Report	Monitoring trend of Bank loans and receivables portfolio	Risk and ALM Committee	Monthly
RAF	Monitoring of risk indicators defined in the RAF	Risk and ALM Committee	Monthly
Risk Reporting	Report containing overall level of Bank risk	Risk and ALM Committee / Board of Directors Bank of Italy	Quarterly
Impairment	Generic and specific assessment of the loans and receivables portfolio	Risk and ALM Committee	Quarterly
Risk Management Report	Report on activity performed, reviews performed, results, measured weaknesses, and actions to be taken for their removal	Risk and ALM Committee/ Bank of Italy	Annual

The Risk Department also produces different reports for internal use and for distribution to other functions. The reports prepared, their scope, their recipients and their frequency are listed as follows:

In particular, Risk Reporting calls for reports on:

- Own Funds and Capital Adequacy
- RWA evolution
- Total Internal Capital
- RAF – Risk Appetite Framework
- Asset Quality
- Total Internal Capital and Stress scenario

With details on

- Credit and counterparty risk
- Pillar 2 risks
- Liquidity and Contingency Funding Plan

Stress testing

The Risk Department performs stress tests to assess the impacts on capital adequacy and other factors generated by a stress scenario.

The stress tests comprise a series of methods of varying complexity and sophistication which make it possible to simulate the sensitivity of the Bank to exceptional but plausible variations in one or more risk factors that could cause deterioration in the financial stability of the Bank.

These consist of:

- **i.** sensitivity analyses, used to measure the adequacy of capital according to variations in just one risk factor;
- **j.** scenario analyses, used to simulate the impact of an adverse shock on assets causing a set of risk factors to change simultaneously. The Risk Department monitors capital adequacy on a monthly basis, partly on the basis of the stress scenarios. The results of the stress scenarios are reported to top management.

It should be noted that, to account for the unique circumstances caused by the COVID-19 emergency, the stress scenarios for 2020 include additional severity elements compared to the scenarios used in previous years.

SECTION 2 – SCOPE OF APPLICATION (ART. 436 CRR)

QUALITATIVE DISCLOSURE

The public disclosure obligations reported in this document apply to Banca Sistema S.p.A. in accordance with Article 19 of Regulation (EU) 575/2013. That regulatory provision allows exempting companies from prudent consolidation if the total amount of assets and off-statement of financial position items involved is less than the lower of either € 10 million or 1% of the total amount of assets and off-statement of financial position items of the entity that owns the equity investment.

At 31 December 2020, the Banca Sistema Group comprised the Parent, Banca Sistema S.p.A., the subsidiaries ProntoPegno S.p.A., Largo Augusto Servizi e Sviluppo S.r.l., and Specialty Finance Trust Holdings Limited, a company incorporated under UK Law, and the Spanish joint venture EBNSistema Finance S.l.u.

All companies have been consolidated using the full line-by-line method except for the joint venture EBNSistema Finance S.l.u. which is consolidated using the equity method.

The scope of consolidation also includes the following special purpose securitisation vehicles whose receivables are not subject to derecognition:

- Quinto Sistema Sec. 2019 S.r.l.
- Quinto Sistema Sec. 2017 S.r.l.
- BS IVA SPV S.r.l.

	Registered office	Type of Relationship (1)	Investment		% of votes avilable (2)
			Investing company	% held	
Companies					
Subject to full consolidation					
S.F. Trust Holdings Ltd	UK	1	Banca Sistema	100%	100%
Largo Augusto Servizi e Sviluppo S.r.l.	Italy	1	Banca Sistema	100%	100%
ProntoPegno S.p.A.	Italy	1	Banca Sistema	75%	75%
EBNSISTEMA Finance S.L.	Spain	7	Banca Sistema	50%	50%

Key:
(1) Type of relationship
(2) Available voting rights at the ordinary Shareholders' Meeting, with separate indication of effective and potential rights

1. = majority of voting rights at the ordinary Shareholders' Meeting
2. = a dominant influence in the ordinary Shareholders' Meeting
3. = agreements with other shareholders
4. = other forms of control
5. = unitary management as defined in Art. 26, paragraph 1 of "Legislative Decree 87/92"
6. = unitary management as defined in Art. 26, paragraph 2 of "Legislative Decree 87/92"
7. = joint control

SECTION 3 – OWN FUNDS
(ART. 437 CRR)

QUALITATIVE DISCLOSURE

Own funds, risk-weighted assets and solvency ratios as at 31 December 2020 were determined based on the new regulation, harmonised for Banks, contained in Directive 2013/36/EU (CRD IV) and in Regulation (EU) 575/2013 (CRR) of 26 June 2013, that transpose in the European Union the standards defined by the Basel Committee on Banking Supervision (the so-called Basel 3 framework), and based upon Bank of Italy Circulars no. 285 and no. 286 (enacted in 2013), and the update of Circular no. 154.

The above regulatory framework provides that own funds have a structure based on two tiers:

- Tier 1 Capital, in turn composed of:
  - Common Equity Tier 1 (CET1) capital;
  - Additional Tier 1 (AT1) capital;
- Tier 2 (T2) capital.

The introduction of the Basel 3 framework was subject to a transitional period, during which the new rules were applied on an expanding basis until 2018, when they were fully applied.

Having met the conditions for inclusion provided for by art. 26(2) of Regulation (EU) no. 575 of 26 June 2013 (CRR), the profit for the year – net of the portion intended for dividends – was included in Common Equity Tier 1 capital, in accordance with board resolutions.

The following table summarises the terms and conditions of Common Equity Tier 1 instruments, Additional Tier 1 instruments and Tier 2 instruments.

Main characteristics of equity instruments					
no.	Characteristics	Ordinary shares	Subordinated Tier 1 bonds	Subordinated lower Tier 2 bonds	Subordinated Tier 2 bonds
1	Issuer	Banca Sistema S.p.A.	Banca Sistema S.p.A.	Banca Sistema S.p.A.	Banca Sistema S.p.A.
2	Unique identifier (ISIN)	IT0003173629	IT0004881444	IT0005247397	IT0005373060
3	Legislation applicable to the instrument	Italian law	Italian law	Italian law	Italian law
Regulatory treatment					
4	Transitional provisions of the CRR	Common Equity Tier 1 Capital	Additional Tier 1 Capital	Tier 2 Capital	Tier 2 Capital
5	Post-transitional provisions of the CRR	Common Equity Tier 1 Capital	Additional Tier 1 Capital	Tier 2 Capital	Tier 2 Capital
6	Admissible at the individual entity level; consolidated level; individual entity and consolidated level	Individual entity and consolidated	Individual entity and consolidated	Individual entity and consolidated	Individual entity and consolidated
7	Type of instrument	Ordinary shares art. 28 CRR	Debt instruments art. 52 CRR	Debt instruments art. 62 CRR	Debt instruments art. 62 CRR
8	Amount included in own funds (€/million)	9.65	8	19.5	18
9	Nominal amount of the instrument (€/million)	N/A	8	19.5	18
9a	Issue price	N/A	At par	At par	At par

Main characteristics of equity instruments					
no.	**Characteristics**	**Ordinary shares**	**Subordinated Tier 1 bonds**	**Subordinated lower Tier 2 bonds**	**Subordinated Tier 2 bonds**
9b	Redemption price	N/A	At par	At par	At par
10	Accounting classification	Equity	Liabilities - amortised cost	Liabilities - amortised cost	Liabilities - amortised cost
11	Original issue date	N/A	- 5 million at 18/12/2012 - 3 million at 18/12/2013	- 14 million at 30/03/2017 - 1.5 million at 5/8/2017 - 1 million at 13/10/2017 - 3 million at 16/04/2018	- 6 million at 23/05/2019 - 12 million at 27/09/2019
12	Unredeemable or at maturity	N/A	Unredeemable	At maturity	At maturity
13	Original maturity date	N/A	Date of dissolution or winding-up of Banca Sistema or due to the lapse of the term provided for by the articles of association (currently the articles of association of Banca Sistema envisage the date of 31 December 2100)	30/03/2027	23/05/2029
14	Early redemption at discretion of issuer after obtaining approval from the supervisory authority	No	Yes	No	No

Main characteristics of equity instruments					
no.	**Characteristics**	**Ordinary shares**	**Subordinated Tier 1 bonds**	**Subordinated lower Tier 2 bonds**	**Subordinated Tier 2 bonds**
15	Date and amount of early redemption	N/A	The issuer reserves the right to early redemption of all or part of the residual nominal amount of the securities beginning on 18 December 2017. Moreover, early redemption clauses connected with tax and/or regulatory events are also envisaged. Early redemption is subject to prior authorisation by the Bank of Italy.	N/A	N/A
16	Subsequent dates of early redemption	N/A	Subsequent to the first date of early redemption, the issuer reserves the right to evaluate whether to proceed with the early redemption on an annual basis	N/A	N/A
Coupons/dividends					

Main characteristics of equity instruments					
no.	**Characteristics**	**Ordinary shares**	**Subordinated Tier 1 bonds**	**Subordinated lower Tier 2 bonds**	**Subordinated Tier 2 bonds**
17	Dividends/fixed- or floating-rate coupons	N/A	Fixed then floating	Floating	Fixed
18	Coupon rate and any correlated indices	N/A	Fixed rate: 7% Floating rate: 6-month Euribor + 5%	6-month Euribor + 5.50%	7%

Main characteristics of equity instruments					
no.	**Characteristics**	**Ordinary shares**	**Subordinated Tier 1 bonds**	**Subordinated lower Tier 2 bonds**	**Subordinated Tier 2 bonds**
19	Presence of a "dividend stopper" mechanism	No	YES	No	3
20a	Fully discretionary, partially discretionary or mandatory (in terms of time)	N/A	Partially discretionary Loss absorption mechanisms that result in the cancellation of any accrued interest and unpaid interest and, if insufficient, a reduction of the residual nominal amount of the securities, are provided for. These mechanisms are generated in those cases where a “capital event” occurs, or when a significant reduction in retained earnings or other reserves occur, thereby triggering a “capital event” in the opinion of the issuer or the supervisory body. The term “capital event” means: a) a reduction of the capital ratios below the minimum regulatory level; b) a drop of the Common Equity Tier 1 ratio below 5.125%. It is also envisaged that the securities be subject to loss absorption measures whenever the Bank of Italy, to the intents and purposes of the regulations in force at the time, deems said measure to be necessary.	N/A	N/A
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	N/A	Partially discretionary	N/A	N/A
21	Presence of "step up" or of other redemption incentive	N/A	No	No	No
22	Non-cumulative or cumulative	N/A	Non-cumulative	N/A	N/A

Main characteristics of equity instruments					
no.	**Characteristics**	**Ordinary shares**	**Subordinated Tier 1 bonds**	**Subordinated lower Tier 2 bonds**	**Subordinated Tier 2 bonds**
23	Convertible or non-convertible	N/A	Non-convertible	Non-convertible	Non-convertible
24	If convertible, event(s) that results(result) in conversion	N/A	N/A	N/A	N/A
25	If convertible, fully or in part	N/A	N/A	N/A	N/A
26	If convertible, conversion rate	N/A	N/A	N/A	N/A
27	If convertible, mandatory or optional conversion	N/A	N/A	N/A	N/A
28	If convertible, specify the type of instrument into which conversion is possible	N/A	N/A	N/A	N/A
29	If convertible, specify the issuer of the instrument into which it is converted	N/A	N/A	N/A	N/A

Main characteristics of equity instruments					
no.	**Characteristics**	**Ordinary shares**	**Subordinated Tier 1 bonds**	**Subordinated lower Tier 2 bonds**	**Subordinated Tier 2 bonds**
30	Impairment mechanisms	N/A	Yes	No	No
31	In case of an impairment mechanism, event(s) that causes (cause) it	N/A	See item 20	N/A	N/A
32	In case of an impairment, full or partial impairment	N/A	Fully or partially	N/A	N/A
33	In case of an impairment, permanent or temporary impairment	N/A	Permanent	N/A	N/A
34	In case of a temporary impairment, description of the revaluation mechanism	N/A	N/A	N/A	N/A

Main characteristics of equity instruments					
no.	**Characteristics**	**Ordinary shares**	**Subordinated Tier 1 bonds**	**Subordinated lower Tier 2 bonds**	**Subordinated Tier 2 bonds**
35	Position in the subordination hierarchy in case of liquidation (specify the type of instrument of immediately senior rank)	N/A	If Banca Sistema is liquidated or subject to insolvency proceedings, the Securities and related rights for principal and interest are (i) subordinated to all unsubordinated creditors of Banca Sistema (including depositors) or those having a lower level of subordination than the level of subordination of the Securities as Tier 2 instruments, (ii) pari passu among them and in relation to additional Tier 1 instruments and other debt exposures of Banca Sistema that do not have a level of subordination that is higher or lower than the Securities, and (iii) senior to the ordinary shares and every class (including any preferred shares and savings shares) of Banca Sistema stock.	The bond was issued with a subordination clause to the intents and purposes of the provisions contained in the supervisory provisions for banks enacted by the Bank of Italy. Therefore, if the issuer is subject to voluntary or compulsory liquidation, the bondholders shall be repaid only after all other creditors of the issuer that do not have the same level of subordination are repaid.	The bond was issued with a subordination clause to the intents and purposes of the provisions contained in the supervisory provisions for banks enacted by the Bank of Italy. Therefore, if the issuer is subject to voluntary or compulsory liquidation, the bondholders shall be repaid only after all other creditors of the issuer that do not have the same level of subordination are repaid.
36	Non-compliant characteristics of the instruments that benefit from transitional measures	N/A	No	No	No
37	If affirmative, specify the non-compliant characteristics	N/A	N/A	N/A	N/A

QUANTITATIVE DISCLOSURE

The following tables show:

- the amount of Own Funds according to the publication format prescribed in Implementing Regulation (EU) No. 143/2013
- the reconciliation of the elements of Own Funds and the Statement of financial position in the Separate Financial Statements of Banca Sistema and the association of the elements of own funds with the respective items listed in the publication format as indicated at the preceding bullet item.

In reference to Own Funds, it is noted that Banca Sistema shares have been traded on the Mercato Telematico Azionario - Italian Equities Market (MTA) of Borsa Italiana, STAR segment, since 2 July 2015.

(Amounts in thousands of Euro)

	Equity items	(A) Amount	(B) Reference article of Regulation (EU) No. 575/2013	(C) Amounts upon full implementation
Common Equity Tier 1 Capital: instruments and reserves				
1	Equity instruments and associated Share Premium Reserves	48,751	26, paragraph 1, 27, 28, 29, EBA list pursuant to art. 26, paragraph 3	48,751
2	Retained earnings	118,198	26, paragraph 1, letter c)	118,198
3	Accumulated other comprehensive income (and other reserves, including unrealised gains and losses pursuant to the applicable accounting regulation)	5,698	26, paragraph 1	5,698
5	Minority interest given recognition in CET1 capital	7,795	84	7,795
5a	Profit for the period verified by independent persons, net of all foreseeable charges or dividends	19,343	26, paragraph 2	19,343
6	Common Equity Tier 1 (CET1) before regulatory adjustments	**199,784**		**199,784**
Common Equity Tier 1 (CET1): regulatory adjustments				
7	Additional value adjustments	-430.966	105	-430.966
8	Intangible assets (net of the relevant tax liabilities) (negative amount)	-32,725	36, paragraph 1, letter b), 37, 472, paragraph 4	-32,725
16	Own Common Equity Tier 1 instruments held directly or indirectly by the issuer (negative amount)	-516.440	36, paragraph 1, letter f), 42	-516.440
	CET1 capital elements or deductions - other*	-2,314		-2,314
26	Regulatory adjustments applied to Common Equity Tier 1 in relation to the amounts subject to pre-CRR treatment			
26a	Regulatory adjustments relative to the unrealised gains and losses pursuant to articles 467 and 468			
	of which unrealised gains on exposures to central governments classified in the "Available for Sale" category of EU-endorsed IAS 39		467	
	of which a filter for unrealised gains		468	
	of which a filter for unrealised losses		467	
28	**Total regulatory adjustments to Common Equity Tier 1 (CET1)**	**-35,987**		**-35,987**
29	**COMMON EQUITY TIER 1 (CET1)**	**163,797**		**163,797**

(*) Following the financial difficulty of a local authority, the Bank used this filter to manage an overdraft position

(Amounts in thousands of Euro)

	Equity items	(A) Amount	(B) Reference article of Regulation (EU) No. 575/2013	(C) Amounts upon full implementation
	Additional Tier 1 (AT1): instruments			
30	Equity instruments and associated Share Premium Reserves	8,000	51, 52	8,000
32	of which classified as liabilities pursuant to the applicable accounting regulation	8,000		8,000
36	**Additional Tier 1 (AT1) before regulatory adjustments**	**8,000**		**8,000**
44	**Additional Tier 1 Capital (AT1)**	**8,000**		**8,000**
45	**Tier 1 Capital (T1=CET1+AT1)**	**171,797**		**171,797**

(Amounts in thousands of Euro)

	Equity items	(A) Amount	(B) Reference article of Regulation (EU) No. 575/2013	(C) Amounts upon full implementation
	Tier 2 Capital (T2): instruments and provisions			
46	Equity instruments and associated Share Premium Reserves	37,500	62, 63	37,500
48	Instruments issued by subsidiaries that are given recognition in T2 Capital	154.964		154.964
51	**Tier 2 Capital (T2) before regulatory adjustments**	**37,655**		**37,655**
58	**Tier 2 Capital (T2)**	**37,655**		**37,655**
59	**Total Capital (TC = T1 + T2)**	**209,452**		**209,452**
60	**Total risk-weighted assets**	**1,297,255**		**1,297,255**
	Capital ratios and buffers			
61	Common Equity Tier 1 (as a percentage of risk exposure)	12.63%	92, paragraph 2, letter a), 465	12.63%
62	Tier 1 capital (as a percentage of risk exposure)	13.24%	92, paragraph 2, letter b), 465	13.24%
63	Total capital (as a percentage of risk exposure)	16.15%	92, paragraph 2, letter c)	16.15%
64	Institution-specific capital buffer requirement (requirement relative to the Common Equity Tier 1 in compliance with article 92, paragraph 1, letter a), capital conservation buffer, countercyclical capital buffer, systemic risk buffer, and systemically important institution buffer in percentage of the risk exposure requirement	2.50%	CRD 128, 129, 130	2.50%
65	of which: capital conservation buffer requirement	2.50%		2.50%

(Amounts in thousands of Euro)

	Assets	Accounting Data	Amount Relevant to Own Funds	Ref. Transitory model table for the publication of information regarding equity funds
100.	Intangible assets	-32,725	-32,725	8
	of which: goodwill	-32,355	-32,355	8
	of which: other intangible assets	-369.935	-369.935	8
	Liabilities	**Accounting Data**	**Amount Relevant to Own Funds**	**Ref. Transitory model table for the publication of information regarding equity funds**
10c	Securities issued	248,338	45,500	30, 32, 46
	of which: subordinated instruments not subject to transitional measures	45,500	45,500	30, 32, 46
120	Valuation reserves	1,287	1,287	3, 26, 26a
	of which: valuation reserves on securities available for sale	1,622	1,622	26, 26a
	of which: other valuation reserves	-335	-355	26, 26a
150	Reserves	122,608	122,608	1, 2
160	Share premium	39,100	39,100	1
170	Share capital	9,651	9,651	1
180	Treasury Shares	-234	-234	5a
200	Profit (loss) for the period	25,777	25,777	5a
	of which: profit for the period net of dividend distributed for the year	6,434	6,434	5a
Total Own Funds at 31 December 2020			**209,452**	

SECTION 4 - CAPITAL REQUIREMENTS
(ART. 438 CRR)

QUALITATIVE DISCLOSURE

According to the provisions of Pillar 2, banks must periodically assess their capital adequacy, current and prospective, expanding the variety of the risks to be calculated with respect to Pillar 1.

This activity is performed as part of the ICAAP/ILAAP process (Internal Capital Liquidity Adequacy Assessment Process), whose responsibility is assigned entirely to the "body responsible for strategic supervision", which independently defines the design and organisation according to its own responsibilities and prerogatives.

The results of the process are subject to analysis on the part of the Supervisory Authorities within the scope of the SREP (Supervisory Review and Evaluation Process).

For the sake of completeness, please note that Directive 2013/36/EU (CRD IV) establishes the obligation for the designated national authorities to activate an operational framework for the definition of the countercyclical capital buffer ratio (CCyB) starting from 1 January 2016. The ratio is subject to quarterly review. The European regulation was implemented in Italy with Circular no. 285 of the Bank of Italy, which contains specific rules applying to CCyB.

The benchmark ratio materially reflects the credit cycle and the risks deriving from excessive growth of credit in Italy, also taking into account the specific nature of the domestic economy. It is based on the deviation from the long-term trend in the ratio between credit and Gross Domestic Product.

The ratio is expressed as a percentage of the total risk exposure of banks that have significant credit exposures on national territory. It is between 0% and 2.5% and is fixed in intervals of 0.25 percentage points or multiples of 0.25. Using the benchmark ratio, the general approach taken by the ESRB, and any other ratio signalling the emergence of systemic risks, the Bank of Italy may set an internal countercyclical ratio higher than 2.5%.

Given the economic and credit situation in Italy, the Supervisory Authority decided to keep the aforementioned ratio at zero also for all of 2020.

For the purposes of a concrete application of the principle of proportionality, the Bank of Italy subdivided the banks into three different classes based on operational size and complexity. Banca Sistema currently falls in class 3, consisting of "banking groups and banks that use standardised approaches, with consolidated or individual assets, respectively, amounting to € 4 billion or less".

The following Pillar 1 and 2 risks are included in the reference scope for the purposes of ICAAP/ILAAP with the relative approaches indicated in the table below:

CATEGORY	TYPE OF RISK	APPROACH
Pillar 1	Credit risk	Standardised Approach
	Counterparty Risk	Standardised Approach (exposure: CRM comprehensive method with supervisory volatility adjustments)
	Market Risk	Standardised Approach
	Operational Risk	Basic Indicator Approach Qualitative Assessment (self-assessment)
	Liquidity Risk	Basel III Indicators (LCR and NSFR)
Pillar 2	Concentration Risk	Granularity Adjustment / Single name ABI-PwC /Geo-Sectoral
	Interest Rate Risk	Standard Approach
	Liquidity Risk	Net financial position
	Reputational Risk	Qualitative Assessment
	Risk of Excessive Leverage	Leverage Ratio
	Strategic Risk	Qualitative Assessment
	Compliance Risk	Qualitative Assessment

The ICAAP/ILAAP is divided into five sub-activities described in detail on the following pages:

1. **Identification and management of material risks**: the competent organisational structures implement the identification process for the risks to which the Bank could be exposed taking into consideration various elements:
   - measuring the statement of financial position aggregates;
   - the Strategic Business Plan, within which the top management illustrates both the short- and medium-term investment policies and objectives;
   - the changed market environment, new opportunities or significant dimensional variations (absolute or relative) of the business components so as to influence positioning in the market and the resulting initial risk assessments;
   - the introduction of new products or services;
   - economic context.

2. **Measurement/assessment of the observed risks and calculation of the relative internal capital:** the Bank defines the risk measurement, assessment and management approaches.

   With reference to Pillar 1 risks, the measurement approaches adopted are those used for prudential supervision purposes.

   With reference to the hard-to-quantify Pillar 2 risks, a judgemental type analysis is performed aimed at defining the valuation and mitigation techniques for the risk considered, in concert with the Bank's other departments.

3. **Calculation of total internal capital and reconciliation with the regulatory capital:** adhering to the provisions of relevant legislation, the Bank calculates the total internal capital in accordance with the building block approach, which consists in adding any internal capital relative to other material risks noted in Pillar 2 to the regulatory requirements in relation to Pillar 1 risks.

   The Bank then conducts the reconciliation operations between total internal capital and regulatory requirements.

4. **Determination of total capital and reconciliation with Own Funds:** the Bank analyses all the statement of financial position items available in order to quantify the total capital available. The following activity consists in reconciling Own Funds and Total Capital.

5. **Management and maintenance of the ICAAP/ILAAP:** the Bank verifies that the total capital is sufficient to cover the previously determined Total Internal Capital requirements. If a situation of insufficiency emerges, the company's top management is promptly informed.

Upon conclusion of the Process, the analysis of capital adequacy is submitted to the attention of the Internal Audit and, for approval, to the Board of Directors.

Upon completion of the ICAAP/ILAAP, the Internal Audit Department issues an opinion that the ICAAP/ILAAP report does not contain material errors with respect to regulatory requirements, while highlighting any anomalies or areas for improvement in a special report that is submitted for approval to the Board of Directors and, afterwards, is sent to the Bank of Italy as an integral part of the documentation supporting the ICAAP/ILAAP. Following the onset of the COVID-19 emergency, in 2020, the Bank, as per the Supervisory Authority's press release of 20 March 2020, submitted its 2019 ICAAP/ILAAP report by the 30 June 2020 deadline.

Through a communication dated 13 April 2021, the Supervisory Authority has requested, for the current year because of the ongoing pandemic, that the ICAAP/ILAAP report on the figures as at 31 December 2020 be submitted by 31 May 2021 instead of the usual deadline of 30 April 2021. In addition to the report, the templates specified in the same communication must also be completed.

QUANTITATIVE DISCLOSURE

(Amounts in thousands of Euro)

Categories/Amounts	Unweighted amounts		Weighted amounts/ requirements	
	31/12/2020	31/12/2019	31/12/2020	31/12/2019
A. EXPOSURES				
A.1 Credit and counterparty risk	**4,285,516**	**4,453,157**	**1,120,413**	**1,236,603**
1. Standardised approach	4,285,516	4,453,157	1,120,413	1,236,603
2. Internal ratings based approach				
2.1 Basic				
2.2 Advanced				
3. Securitisations				
B. CAPITAL REQUIREMENTS				
B.1 Credit and counterparty risk			**89,633**	**98,928**
B.2 Credit valuation adjustment risk				**3**
B.3 Settlement risk				
B.4 Market risk				
1. Standard approach				
2. Internal models				
3. Concentration risk				
B.5 Operational risk			**14,147**	**13,540**
1. Basic indicator approach			14,147	13,540
2. Standardised approach				
3. Advanced measurement approach				
B.6 Other calculation elements				
B.7 Total prudential requirements			**103,780**	**112,471**
C. EXPOSURES AND CAPITAL RATIOS			**1,297,255**	**1,405,890**
C.1 Risk-weighted assets			1,297,255	1,405,890
C.2 CET1 capital/risk-weighted assets (CET1 Capital Ratio)			12.6%	11.7%
C.3 Tier 1 capital/risk-weighted assets (Tier 1 Capital Ratio)			13.2%	12.3%
C.4 Total Own Funds/risk-weighted assets (Total Capital Ratio)			16.1%	15.0%

Under the Supervisory Review and Evaluation Process ("2019 SREP Decision"), to ensure compliance with binding provisions even in the face of an economic and financial downturn, the Banca Sistema Group, starting from the reporting of own funds as at 31.03.2020, is required to comply with the following capital ratios at consolidated level:

- **CET1 Ratio** of 7.75%, which consists of a binding component of 5.25% (of which 4.5% for the minimum regulatory requirements and 0.75% to cover the additional requirements determined upon completion of the SREP) and, for the remainder, of the capital conservation buffer component
- **Tier 1 Ratio** of 9.55%, which consists of a binding component of 7.05% (of which 6% for the minimum regulatory

requirements and 1.05% to cover the additional requirements determined upon completion of the SREP) and, for the remainder, of the capital conservation buffer component

- **Total Capital Ratio** of 11.90%, which consists of a binding component of 9.40% (of which 8% for the minimum regulatory requirements and 1.40% to cover the additional requirements determined upon completion of the SREP) and, for the remainder, of the capital conservation buffer component.

These capital ratios correspond to the Overall Capital Requirement (OCR) ratios as defined in the Guidelines and represent the sum of the binding provisions (Total SREP Capital Requirement ratio - TSCR) and the combined capital buffer requirement.

Moreover, the Banca Sistema Group has not exercised the right granted under Art. 473a of Regulation (EU) no. 575/2013 (CRR), which concerns the transitional provisions aimed at mitigating the impact of the introduction of IFRS 9. Consequently, it has not filled out the "IFRS 9-FL Template", whose purpose is to give a comparison between own funds, CET1, Tier 1 Capital, risk-weighted assets, the CET1 Ratio, the Tier 1 Ratio, the Total Capital Ratio, and the Leverage Ratio of institutions, with and without application of the transitional provisions for IFRS 9 or similar expected losses on loans.

SECTION 5 - EXPOSURE TO COUNTERPARTY CREDIT RISK
(ART. 439 CRR)

QUALITATIVE DISCLOSURE

The Bank pays adequate attention to counterparty risk understood as the risk that the counterparty of a transaction – regarding specific financial instruments such as over the counter derivatives, repurchase agreements and reverse repurchase agreements on securities or commodities, security or commodity borrowing or lending transactions and Security Financing Transactions, transactions with long-term settlement in which one of the counterparties pledges to sell or purchase a security, a commodity, a foreign currency against the collection or payment of cash on a contractually established settlement date after that defined by market practice for transactions of same type – may default.

This particular type of credit risk generates a bilateral-type exposure, due to which both counterparties are exposed to the risk of incurring unforeseeable losses.

The Bank conducts a careful and balanced counterparty risk management, establishing an adequate system of limits in terms of consistency and composition of its securities portfolio. With reference to the repurchase agreement positions, the Bank operates having as its counterparty the Compensation and Guarantee Fund (being an indirect participant, Banca Sistema avails itself of the clearing system provided by the depositary bank) or institutional counterparties.

As at 31 December 2020, only repurchase agreements are outstanding with the Compensation and Guarantee Fund.

QUANTITATIVE DISCLOSURE

OUTSTANDING REPURCHASE AGREEMENTS

(Amounts in thousands of Euro)

Type of instrument	Regulatory trading book	Banking book
Reverse repurchase agreements		5,546
Repurchase agreements		235,230

SECTION 8 – CREDIT RISK ADJUSTMENTS (ART. 442 CRR)

QUALITATIVE DISCLOSURE

The Banca Sistema Group defined its credit quality policy based on the provisions in the Bank of Italy Circular no. 272 (Accounts matrix), the main definitions of which are provided on the following pages. The policy is being reviewed in accordance with the provisions of update no. 13 of the aforementioned circular, which transposes the European regulations on the new definition of default[6].

The Supervisory Provisions for Banks impose specific obligations on intermediaries for the monitoring and classification of loans:

“The compliance measures adopted by operating units while the disbursed loan is being monitored must be derived from internal regulations. In particular, the terms and methods of action must be set in the event of anomalies. The criteria for measurement, management and classification of irregular loans, as well as the related responsible units, must be set through a resolution by the Board of Directors in which the methods for connecting these criteria with those required for the supervisory reports are indicated. The Board of Directors must be regularly informed on the performance of the irregular loans and the related recovery procedures.” According to the definitions in the above-mentioned Bank of Italy Circular, “non-performing” financial assets are defined as those that lie within the “bad exposures”, “unlikely to pay” or “past due and/or overdrawn exposures” categories.

Exposures whose anomalous situation is attributable to factors related to “country risk” are not included in “non-performing” financial assets.

The key definitions are shown as follows.

Bad exposures

On- and off-statement of financial position exposures (loans, securities, derivatives, etc.) owed by a party in state of insolvency (even if not judicially ascertained) or in broadly similar situations, regardless of any loss forecast formulated by the Group (cf. art. 5 bankruptcy law). The definition therefore applies regardless of the existence of any collateral or personal guarantee provided as protection against the exposures. This class also includes:

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

b. receivables acquired from third parties in which the main debtors are non-performing, regardless of the portfolio’s accounting allocation.

Unlikely to pay

The classification in this category is first and foremost based on the Bank’s judgement regarding the unlikelihood that, without having to resort to actions such as enforcing the guarantees, the debtor will completely (with regard to principal and/or interest) fulfil its credit obligations. This assessment is made independently of whether any sums (or instalments) are past due and not paid. It is therefore unnecessary to wait for explicit symptoms of irregularity (non-repayment) if there are elements that entail a situation of default risk on the part of the debtor (e.g. a crisis in the industrial sector in which the debtor operates). The set of on- and off-statement of financial position exposures to the same debtor in the above conditions is named “unlikely to pay”, unless the conditions for classifying the debtor under bad exposures exist.

(6) Commission Delegated Regulation (EU) 171/2018 of 19 October 2017 with regard to the materiality threshold for credit obligations past due and Guidelines on the application of the definition of default under Article 178 of Regulation (EU) No 575/2013 (EBA/GL/2016/07).

Past due and/or overdrawn exposures

These are understood to be the on-statement of financial position exposures at carrying amount and off-statement of financial position exposures (loans, securities, derivatives, etc.), other than those classified as bad exposures and unlikely to pay, that, on the reference date of the report, have been past due or have been overdrawn by more than 90 days.

In order to verify the continuity of the past due exposure in connection with factoring transactions, the following should be noted:

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

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

The regulation requires that the debtor’s total exposure be considered past due and/or overdrawn, on the reference date of the report, any time the 5% materiality level is exceeded.

Forborne exposures

Forborne exposures are defined as exposures that fall into the category “Non-performing exposures with forbearance measures” and “Forborne performing exposures” as defined by the Implementing Technical Standards (ITS).

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

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

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

- a modified contract was classified as non-performing or would in the absence of modification be classified as non-performing;
- the modification made to a contract involves a total or partial cancellation by write-offs of the debt;
- the institution approves the use of embedded forbearance clauses for a debtor who is under non-performing status or who would be considered as non-performing without the use of these clauses;
- simultaneously with or close in time to the concession of additional debt by the institution, the debtor made payments

of principal or interest on another contract with the institution that was non-performing or would in the absence of refinancing be classified as non-performing.

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

- the modified contract was totally or partially past-due by more than 30 days (without being non-performing) at least once during the three months prior to its modification or would be more than 30 days past-due, totally or partially, without modification;
- simultaneously with or close in time to the concession of additional debt by the institution, the debtor made payments of principal or interest on another contract with the institution that was totally or partially 30 days past due (without being non-performing) at least once during the three months prior to its modification or would be more than 30 days past-due, totally or partially, without modification;
- the institution approves the use of embedded forbearance clauses for 30 days past-due debtors or debtors who would be 30 days past-due without the exercise of these clauses.

During 2014, the IASB issued the new financial reporting standard "IFRS9: Financial Instruments", replacing IAS 39 and in force from 1 January 2018. The final version of the new IFRS9 requires that banks revise their financial instrument management processes and criteria in terms of:

- "Classification and Measurement": a new classification method based on analysis of the business model for the management of financial assets and related contractual cash flows. According to the results of those analyses, the assets are measured at: Amortised cost, fair value through other comprehensive income (FVOCI); fair value through profit or loss (FVTPL). In this case, reference should be made to the Business Model Policy issued by the Bank

- "Impairment", whose principal changes concern:

a. the introduction of an impairment model based on expected credit loss, with the adoption of a forward looking approach;

b. the classification of financial instruments into three stages of credit quality and the consequent need to establish a specific "Stage Assignment Framework";

c. the calculation of impairment losses according to the assigned credit quality stage.

- "Hedge Accounting".

The Stage Assignment Framework adopted by Banca Sistema sets out the requirements needed to classify financial instruments on the basis of supervening "deterioration" in credit quality, in accordance with the requirements of IFRS9, i.e. with a method that is consistent among the various portfolios and within the Bank. The classification into growing stages of risk is assessed by using all the significant information contained in current processes, including credit monitoring (i.e. "reasonable and supportable information that is available without undue cost and effort"), in addition to any updates.

The method consists in the classification of financial assets in three stages of increasing risk, which correspond to the different methods for measuring impairment losses according to the uniform concept of "expected credit losses" (ECL). For this purpose, Banca Sistema has implemented a model for the calculation of provisions covering expected losses on financial instruments based on:

- the portion of lifetime ECL resulting from possible default events within the 12 months after the reporting date, or over a shorter period when the expected contractual duration is shorter (Stage 1);
- the estimate of the lifetime ECL, when the credit risk of the credit instrument is deemed to have increased significantly after

initial recognition (Stage 2).

So, the Stage Assignment Framework requires classifying the performing financial instruments in two different stages, with each one representing an increasing level of risk:

- Stage 1 contains all performing loans that, whether originated or purchased, have not undergone an "SICR" or, although their credit risk has changed over time, they are characterised by a low level of credit risk at the reporting date;
- Stage 2 contains the loans and receivables which, at the reporting date, have had an SICR since their initial recognition and that risk level is no longer considered to be low.

Classification in Stage 3 is instead required for all relationships in default at the reporting date according to the definition of non-performing loan given in current regulatory instructions, and thus aligned with the 7th update to Bank of Italy Circular no. 272 of 30 July 2008, i.e. those which have the characteristics mentioned in paragraph B5.5.37 of IFRS9, which correspond to the "FINAL draft Implementing Technical Standards" ("ITS") containing the implementing technical standards on forbearance (FBE) and non-performing exposures (EBA/ITS /2013/03/rev1 24/7/2014). Moreover, Stage 3 maintains without any changes the classification into administrative stages of credit quality pursuant to Bank of Italy regulations.

The loans and receivables measurement process is carried out in the following steps:

- **identification**, in the loans and receivables portfolio, of objective evidence of impairment (in Stage 3) or a supervening significant increase in credit risk (in Stage 2);
- **analysis** of the significance of the individual asset subject to impairment. In particular, after having found objective evidence of impairment of the loans and receivables portfolio, the measurement process must determine whether that evidence refers to: a single significant exposure, which necessarily has to be subject to an individual measurement process;
- **measurement** of the impairment on an individual basis (**individual measurement**) or by uniform classes of assets (**collective measurement**).

The loans and receivables that do not show objective evidence of impairment, and as such are not subject to individual measurement, or the loans and receivables for which the individual measurement process produces a forecast of full recovery, must undergo a collective measurement process (Stage 1 or Stage 2 scope).

The accounting standard requires that in the case of non-performing loans, including those for which the measurement process produces a forecast of full recovery, are subject to individual impairment, which is determined individually or through the use of predetermined percentages.

The loans and receivables classified in Stage 3 and in the following risk classes defined in Bank of Italy Circular no. 272/08 are subject to individual impairment:

- Bad exposures
- Unlikely to pay
- More than 90 days past due

QUANTITATIVE DISCLOSURE

The tables shown in the following Schedule were taken from the Financial Statements at 31 December 2020, part E of the Notes to the Financial Statements. It is deemed that the period-end values are representative of the Bank's risk exposures during the relevant period.

BREAKDOWN OF FINANCIAL ASSETS BY PORTFOLIO AND BY CREDIT QUALITY (CARRYING AMOUNTS)

(Amounts in thousands of Euro)

	Portfolios/quality	Bad exposures	Unlikely to pay	Non-performing past due exposures	Other non-performing exposures	Performing exposures	Total
1.	Financial assets measured at amortised cost	27,114	128,080	49,942	546,227	2,391,428	3,142,791
2.	Financial assets measured at fair value through other comprehensive income					425,348	425,348
3.	Financial assets designated at fair value through profit or loss						
4.	Other financial assets mandatorily measured at fair value through profit or loss						
5.	Financial assets held for sale						
Total at 31.12.2020		**27,114**	**128,080**	**49,942**	**546,227**	**2,816,776**	**3,568,139**
Total at 31.12.2019		**30,544**	**123,306**	**54,549**	**709,093**	**2,745,115**	**3,662,607**

BREAKDOWN OF FINANCIAL ASSETS BY PORTFOLIO AND BY CREDIT QUALITY
(GROSS AMOUNT AND CARRYING AMOUNT)

(Amounts in thousands of Euro)

	Portfolios/quality	Non-performing				Performing			Total (carrying amount)
		Gross amount	Total impairment losses	Carrying amount	Overall partial write-offs	Gross amount	Total impairment losses	Carrying amount	
1.	Financial assets measured at amortised cost	251,165	46,028	205,137		2,946,707	9,016	2,937,655	3,142,791
2.	Financial assets measured at fair value through other comprehensive income					425,554	206	425,348	425,348
3.	Financial assets designated at fair value through profit or loss					X	X		
4.	Other financial assets mandatorily measured at fair value through profit or loss					X	X		
5.	Financial assets held for sale								
Total at 31.12.2020		**251,165**	**46,028**	**205,137**		**3,372,261**	**9,222**	**3,363,003**	**3,568,139**
Total at 31.12.2019		**245,616**	**37,217**	**208,399**		**3,460,195**	**5,988**	**3,454,208**	**3,662,607**

ON- AND OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES WITH BANKS:

(Amounts in thousands of Euro)

Type of exposure / amounts		Gross amount		Total impairment and allowances	Carrying amount	Overall partial write-offs
		Non-performing	Performing			
A.	**ON-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES**					
a)	Bad exposures		X			
	- of which: forborne exposures		X			
b)	Unlikely to pay		X			
	- of which: forborne exposures		X			
c)	Non-performing past due exposures		X			
	- of which: forborne exposures		X			
d)	Performing past due exposures	X				
	- of which: forborne exposures	X				
e)	Other performing exposures	X	92,500	20	92,480	
	- of which: forborne exposures	X				
TOTAL A			**92,500**	**20**	**92,480**	
B.	**OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES**					
a)	Non-performing		X			
b)	Performing	X	2,446		2,446	
TOTAL B			**2,446**		**2,446**	
TOTAL A+B			**94,946**	**20**	**94,926**	

On-statement of financial position loans and receivables with banks - gross non-performing exposures subject to "country risk": On-statement of financial position loans and receivables with banks are all performing.

On-statement of financial position loans and receivables with banks - changes in impaired positions: There are no non-performing loans and receivables with banks.

ON- AND OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES WITH CUSTOMERS: GROSS AMOUNTS AND CARRYING AMOUNTS

(Amounts in thousands of Euro)

Type of exposure / amounts		Gross amount		Total impairment and allowances	Carrying amount	Overall partial write-offs
		Non-performing	Performing			
A.	**ON-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES**					
a)	Bad exposures	52,354	X	25,241	27,113	
	- of which: forborne exposures	369	X	369		
b)	Unlikely to pay	148,433	X	20,352	128,080	
	- of which: forborne exposures	296	X	118	177	
c)	Non-performing past due exposures	50,377	X	435	49,942	
	- of which: forborne exposures		X			
d)	Performing past due exposures	X	548,786	2,560	546,226	
	- of which: forborne exposures	X				
e)	Other performing exposures	X	2,733,328	6,679	2,726,649	
	- of which: forborne exposures	X	1,062	7	1,055	
TOTAL A		**251,164**	**3,282,115**	**55,268**	**3,478,011**	
B.	**OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES**					
a)	Non-performing	10,389	X		10,389	
b)	Performing	X	229,592	26	450,176	
TOTAL B		**10,389**	**229,592**	**26**	**460,565**	
TOTAL A+B		**261,553**	**3,511,707**	**55,294**	**3,938,576**	

ON-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES WITH CUSTOMERS: GROSS NON-PERFORMING EXPOSURES

(Amounts in thousands of Euro)

Reasons/Categories		Bad exposures	Unlikely to pay	Non-performing past due exposures
A.	**Opening gross balance**	**50,622**	**139,348**	**55,646**
	- of which: positions transferred but not derecognised			
B.	**Increases**	**16,505**	**193,225**	**207,750**
	B.1 transfers from performing loans	2,630	11,643	119,325
	B.2 transfers from purchased or originated credit-impaired financial assets	821	13,175	20
	B.3 transfers from other categories of non-performing exposures	998	4,781	
	B.4 contract amendments without derecognition			
	B.5 other increases	12,056	163,626	88,405
C.	**Decreases**	**14,773**	**184,141**	**213,019**
	C.1 transfers to performing loans	1,564	596	86,399
	C.2 write-offs	455		
	C.3 collections	12,754	182,824	121,562
	C.4 gains on sales			
	C.5 losses on sales			
	C.6 transfers to other categories of non-performing exposures		722	5,058
	C.7 contract amendments without derecognition			
	C.8 other decreases			
D.	**Closing gross balance**	**52,354**	**148,433**	**50,377**
	- of which: positions transferred but not derecognised	8	718	3,875

ON-STATEMENT OF FINANCIAL POSITION NON-PERFORMING LOANS AND RECEIVABLES WITH CUSTOMERS: CHANGES IN IMPAIRED POSITIONS

(Amounts in thousands of Euro)

	Reasons/Categories		Bad exposures	Unlikely to pay	Non-performing past due exposures
A.	**Opening gross balance**		**50,622**	**139,348**	**55,646**
	- of which: positions transferred but not derecognised				
B.	**Increases**		**16,505**	**193,225**	**207,750**
	B.1	transfers from performing loans	2,630	11,643	119,325
	B.2	transfers from purchased or originated credit-impaired financial assets	821	13,175	20
	B.3	transfers from other categories of non-performing exposures	998	4,781	
	B.4	contract amendments without derecognition			
	B.5	other increases	12,056	163,626	88,405
C.	**Decreases**		**14,773**	**184,141**	**213,019**
	C.1	transfers to performing loans	1,564	596	86,399
	C.2	write-offs	455		
	C.3	collections	12,754	182,824	121,562
	C.4	gains on sales			
	C.5	losses on sales			
	C.6	transfers to other categories of non-performing exposures		722	5,058
	C.7	contract amendments without derecognition			
	C.8	other decreases			
D.	**Closing gross balance**		**52,354**	**148,433**	**50,377**
	- of which: positions transferred but not derecognised		8	718	3,875

BREAKDOWN BY BUSINESS SEGMENT OF ON- AND OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES WITH CUSTOMERS

(Amounts in thousands of Euro)

Exposures/Counterparties	Public administrations		Financial companies		Financial companies (of which: insurance companies)		Non-financial companies		Households	
	Carrying amount	Total impairment	Carrying amount	Total impairment	Carrying amount	Total impairment	Carrying amount	Total impairment	Carrying amount	Total impairment
A. On-statement of financial position loans and receivables										
A.1 Bad exposures	17,811	1,143					9,147	23,501	155	597
- of which: forborne exposures								369		
A.2 Unlikely to pay	98,323	7,255					27,167	10,947	2,590	2,150
- of which: forborne exposures							177	118		
A.3 Non-performing past due exposures	26,147	193	7		5		16,021	157	7,767	85
- of which: forborne exposures							587	176		
A.4 Performing exposures	1,853,656	4,117	90,207	1,538	9		298,562	1,768	1,028,194	1,816
- of which: forborne exposures										
Total (A)	**1,995,937**	**12,708**	**90,213**	**1,538**	**14**		**350,896**	**36,373**	**1,038,706**	**4,648**
B. Off-statement of financial position loans and receivables										
B.1 Non-performing exposures	3,250				10		7,139			
B.2 Performing exposures	220,610		109,919		10		117,014	26	2,614	
Total (B)	**223,860**		**109,919**		**20**		**124,152**	**26**	**2,614**	
Total (A+B) at 31.12.2020	**2,219,797**	**12,708**	**200,132**	**1,538**	**34**		**475,049**	**36,399**	**1,041,320**	**4,648**
Total (A+B) at 31.12.2019	**2,385,555**	**9,903**	**193,380**	**57**	**12**		**388,287**	**29,923**	**861,991**	**3,338**

BREAKDOWN BY GEOGRAPHICAL SEGMENT OF ON- AND OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES WITH CUSTOMERS

(Amounts in thousands of Euro)

Exposures/Geographical areas	Italy		Other European countries		America		Asia		Rest of the world	
	Carrying amount	Total impairment losses	Carrying amount	Total impairment losses	Carrying amount	Total impairment losses	Carrying amount	Total impairment losses	Carrying amount	Total impairment losses
A. On-statement of financial position loans and receivables										
A.1 Bad exposures	27,113	25,161								
A.2 Unlikely to pay	128,080	20,352								
A.3 Non-performing past due exposures	49,942	435								
A.4 Performing exposures	3,206,768	7,481	63,059	1,817	2,754	17	533	3	261	2
Total (A)	**3,411,404**	**53,429**	**63,059**	**1,817**	**2,754**	**17**	**533**	**3**	**261**	**2**
B. Off-statement of financial position loans and receivables										
B.1 Non-performing exposures	10,389									
B.2 Performing exposures	436,503	10	11,172				2,500	16		
Total (B)	**446,892**	**10**	**11,172**				**2,500**	**16**		
Total (A+B) at 31.12.2020	**3,858,296**	**53,439**	**74,231**	**1,817**	**2,754**	**17**	**3,034**	**19**	**261**	**2**
Total (A+B) at 31.12.2019	**3,758,458**	**43,020**	**57,099**	**198**	**1,094**	**4**			**46**	

BREAKDOWN OF FINANCIAL ASSETS AND LIABILITIES BY REMAINING CONTRACTUAL TERM

(Amounts in thousands of Euro)

	Item/Time buckets	on demand	from more than 1 day up to 7 days	from more than 7 days up to 15 days	from more than 15 days up to 1 month	from more than 1 month up to 3 months	from more than 3 months up to 6 months	from more than 6 months up to 1 year	from more than 1 year up to 5 years	over 5 years	Open term
A.	**Assets**	**1,258,756**	**7,121**	**2,617**	**27,279**	**94,337**	**369,327**	**316,346**	**1,054,511**	**328,767**	**40,269**
A.1	Government securities			28		21	265,231	192,961	415,192		
A.2	Other debt instruments				64		64	128	3,129	2,609	
A.3	OEIC units										
A.4	Financing	1,258,756	7,121	2,589	27,215	94,316	104,032	123,257	636,190	326,158	40,269
	- banks	51,319			34	1	1	3	1		40,269
	- customers	1,207,437	7,121	2,589	27,182	94,316	104,031	123,254	636,189	326,158	
B.	**Liabilities**	**727,198**	**253,506**	**35,547**	**25,865**	**274,019**	**231,257**	**688,014**	**884,304**	**164,052**	
B.1	Deposits and current accounts	648,667	8,156	35,405	25,807	272,081	135,090	477,307	350,921	24,628	
	- banks	953		30,000	15,000	50,000	30,000				
	- customers	647,714	8,156	5,405	10,807	222,081	105,090	477,307	350,921	24,628	
B.2	Debt instruments					390	93,447	1,316		45,500	
B.3	Other liabilities	78,531	245,350	142	58	1,547	2,720	209,391	533,383	93,923	
C.	**Off-statement of financial position transactions**	**79,720**			**58**	**9**		**56**	**4,358**	**20**	
C.1	Financial derivatives with exchange of principal										
	- long positions										
	- short positions										
C.2	Financial derivatives without exchange of principal										
	- long positions										
	- short positions										
C.3	Deposits and financing to be received										
	- long positions										
	- short positions										
C.4	Irrevocable commitments to disburse funds	77,273			58			56	119		
	- long positions	38,520			58			56	119		
	- short positions	38,753									
C.5	Financial guarantees issued	2,446				9			4,239	20	
C.6	Financial guarantees received										
C.7	Credit derivatives with exchange of principal										
	- long positions										
	- short positions										
C.8	Credit derivatives without exchange of principal										
	- long positions										
	- short positions										

BREAKDOWN BY GEOGRAPHICAL SEGMENT OF ON- AND OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES WITH BANKS

(Amounts in thousands of Euro)

Exposures/Geographical areas	Italy		Other European countries		America		Asia		Rest of the world	
	Carrying amount	Total impairment losses	Carrying amount	Total impairment losses	Carrying amount	Total impairment losses	Carrying amount	Total impairment losses	Carrying amount	Total impairment losses
A. On-statement of financial position loans and receivables										
A.1 Bad exposures										
A.2 Unlikely to pay										
A.3 Non-performing past due exposures										
A.4 Performing exposures	93,980	20								
Total (A)	**93,980**	**20**								
B. Off-statement of financial position loans and receivables										
B.1 Non-performing exposures										
B.2 Performing exposures	2,446									
Total (B)	**2,446**									
Total A+B at 31.12.2020	**96,427**	**20**								
Total A+B at 31.12.2019	**83,839**	**26**	**117**							

At 31 December 2020, the Large Exposures of the Parent (exposures equal to or greater than 10% of Own Funds) consist of 16 positions for a sum of:

a. Carrying amount € 1,821,836 (in thousands)

b. Weighted value € 193,312 (in thousands)

SECTION 9 – UNENCUMBERED ASSETS
(ART. 443 CRR)

QUALITATIVE DISCLOSURE

The encumbered assets of the Bank include debt instruments pledged as security for refinancing operations at the ECB and debt instruments used as collateral in repurchase agreements. The encumbered assets also include trade receivables as security c/o the Central Bank via ABACO.

In order to avoid excessive recourse to overcollateralisation of the securities available, the Bank, starting from 2016, consistent with the prudential supervisory provisions, established, within the purview of the Risk Appetite Framework, that an adequate level of readily monetizable assets be available in line with the business outlook, as forecast by the 2020 budget.

As at 31 December 2020, the encumbered debt instruments amounted to approximately € 353.4 million, while the carrying amount of the credits in ABACO and the security deposit with Cassa Depositi e Prestiti fell mainly among the other encumbered assets (€ 745.6 million).

Table C shows the amount of liabilities associated with the encumbered assets and guarantees received which can be associated with repurchase agreements.

In accordance with the regulations issued by the EBA, institutions have to indicate the quantities of encumbered and unencumbered assets, broken down by type of asset, on the statement of financial position that have been posted as collateral or transferred without derecognition or otherwise encumbered, and the received guarantees that meet the conditions for recognition in the transferee's financial statements.

QUANTITATIVE DISCLOSURE

MODEL A – ENCUMBERED ASSETS

(Amounts in thousands of Euro)

	Carrying amount of the encumbered assets	Fair value of the encumbered assets	Carrying amount of the unencumbered assets	Fair value of the unencumbered assets
Assets of the reporting institution	1,098,994		2,572,376	
Equity instruments			5,404	5,404
Debt instruments	353,400	353,400,459	528,370	528,369
Other assets	745,594		2,038,602	

MODEL B - COLLATERAL RECEIVED

(Amounts in thousands of Euro)

	Fair value of the encumbered collateral received or of the own debt instruments issued	Fair value of the collateral received or of the own debt instruments issued and which could be encumbered
Collateral received by the reporting institution		
Equity instruments		
Debt instruments		5,542
Other collateral received		
Own debt instruments issued other than own secured bonds or ABS		

MODEL C - ENCUMBERED ASSETS/COLLATERAL RECEIVED AND ASSOCIATED LIABILITIES

(Amounts in thousands of Euro)

	Liabilities corresponding to contingent liabilities or securities loaned	Assets, collateral received and debt instruments issued other than secured bonds and encumbered ABS
Carrying amount of selected financial liabilities	924,915	1,089,524

SECTION 10 – USE OF ECAIS

(ART. 444 CRR)

QUALITATIVE DISCLOSURE

Banca Sistema calculates the capital requirement with respect to credit risk based on the standardised approach.

As at 31 December 2020, the Bank availed itself of the rating issued by the ECAI:

- "Dominion Bond Rating Service" (DBRS), for exposures to: central authorities and central banks; supervised brokers; public sector institutions and territorial entities;
- "Fitch Ratings", with regard to exposures to businesses and other parties.

The identification of a reference ECAI does not represent in any way, in subject matter or in purposes, an assessment on the merit of the opinions made by the ECAI or a support of the methodologies used, for which the External Credit Assessment Institutions remain solely responsible.

QUANTITATIVE DISCLOSURE

The following table shows the breakdown of exposures subject to credit risk based on the weighting factors (credit rating classes). The total of € 4,332,575 thousand represents the sum of the "On-statement of financial position exposures" and "Off-statement of financial position exposures" reported in the table in section 19.

(Amounts in thousands of Euro)

Regulatory class	Weighting								Total
	0%	20%	35%	50%	75%	100%	150%	250%	
Central authorities and central banks	1,354,551					3,950		6,343	**1,364,844**
Territorial entities, public sector institutions, non-profit entities	37,339	762,903				20,476			**820,719**
Supervised brokers		395,100				3,129			**398,229**
Multilateral development banks									
International organisations									
Companies and other parties		2.442				448,248			**448,250**
Retail			853,374		165,358				**1,018,732**
OEIC units									
Securitisations									
Covered bonds									
Exposures secured by properties			1,512						**1,512**
Exposures in equity instruments						6,618			**6,618**
Non-performing exposures						24,020	185,923		**209,942**
Other exposures	5,387					52,702	5,641		**63,730**
Total									**4,332,575**

SECTION 11 – EXPOSURE TO MARKET RISK (ART. 445 CRR)

QUALITATIVE DISCLOSURE

Market risk represents the downside risk deriving from adverse changes in market prices (stock prices, interest rates, exchange rates, commodity prices, risk factor volatility, etc.) related to the regulatory trading book (position, regulatory and concentration risks) and to the entire accounts of the Bank (foreign exchange risk and commodity position risk).

Banca Sistema calculates the capital requirement with respect to market risk based on the standardised approach.

The regulation identifies and governs the treatment of different types of market risk related to the regulatory trading book. As at 31 December 2020, the Bank was not exposed to market risk.

SECTION 12 – OPERATIONAL RISK (ART. 446 CRR)

QUALITATIVE DISCLOSURE

Operational risk is the risk of loss arising from inadequate or non-functioning internal processes, human resources or systems, or from external events. This type of risk includes the following events:

- fraud;
- human errors;
- business disruption;
- unavailability of systems;
- inadequate execution of processes;
- breaches of contract;
- natural catastrophes etc.

Operational risk includes legal risk, whereas it does not include strategic risks and reputational risks. Operational risk, therefore, refers to other types of events that, under present conditions, would not be individually relevant if not analysed jointly and quantified for the entire risk category.

In order to determine the capital requirement to hedge operational risk, the Bank adopts the Basic Indicator Approach, which envisages that the capital requirement be calculated applying a regulatory coefficient equal to 15% of the three-year average of the relevant indicator established in article 316 of Regulation (EU) no. 575/2013.

As an additional oversight of operational risk, the Bank has opened an insurance policy on operational risks deriving from actions of third parties or caused to third parties, as well as suitable riders to cover the damages caused by suppliers of infrastructures and services, and it approved a Business Continuity Plan.

The Bank, in order to counter the effects of COVID-19 and to comply with the regulations issued by the Government, has adopted the measures described in the Memorandums of Understanding on workplace safety ("Shared Memorandum regulating measures to counter and contain the spread of the COVID-19 virus in the workplace", signed on 14 March between the social partners, and the "Shared Memorandum for measures to prevent, counter and contain the spread of the COVID-19 virus in the banking sector" signed on 16 March 2020 between ABI and the trade unions of the sector, as amended).

QUANTITATIVE DISCLOSURE

On the basis of the approach illustrated above, the capital requirement covering operational risk at 31 December 2020 was € 14.1 million.

SECTION 13 – EXPOSURES IN EQUITIES NOT INCLUDED IN THE TRADING BOOK (ART. 447 CRR)

QUALITATIVE DISCLOSURE

Investments in equities, included in the banking book, pursue a plurality of objectives such as: strategic, institutional, financial investment and support for operations. Accounting techniques:
The exposures in equity instruments included in the banking book are classified in the financial statement items Equity investments and Financial assets measured at fair value through other comprehensive income.

Financial assets measured at fair value through other comprehensive income (FVOCI).

Classification criteria

This category includes the financial assets that meet both the following conditions:

- financial assets that are held under a business model whose aim is achieved both through the collection of contractual cash flows and through sale ("Held to Collect and Sell" business model);
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding ("SPPI Test" passed).

This item also includes equity instruments, not held for trading, for which the option was exercised upon initial recognition of their designation at fair value through other comprehensive income.
In particular, this item includes:

- debt instruments that can be attributed to a Held to Collect and Sell business model and that have passed the SPPI test;
- equity interests, that do not qualify as investments in subsidiaries, associates or joint ventures and are not held for trading, for which the option has been exercised of their designation at fair value through other comprehensive income.

Except for the equity instruments which cannot be reclassified, financial assets may be reclassified to other categories of financial assets only if the entity changes its own business model for management of the financial assets.
In such cases, which are expected to be absolutely infrequent, the financial assets may be reclassified from those measured at fair value through other comprehensive income to one of the other two categories established by IFRS 9 (Financial assets measured at amortised cost or Financial assets measured at fair value through profit or loss). The transfer value is the fair value at the time of the reclassification and the effects of the reclassification apply prospectively from the reclassification date. In the event of reclassification from this category to the amortised cost category, the cumulative gain (loss) recognised in the valuation reserve is allocated as an adjustment to the fair value of the financial asset at the reclassification date. In the event of reclassification to the fair value through profit or loss category, the cumulative gain (loss) previously recognised in the valuation reserve is reclassified from equity to profit (loss).

- **Recognition criteria**

  Initial recognition of the financial assets is at the date of disbursement, based on their fair value including the transaction costs/income directly attributable to the acquisition of the financial instrument. Costs/income having the previously mentioned characteristics that will be repaid by the debtor or that can be considered as standard internal administrative costs are excluded.
  The initial fair value of a financial instrument is usually the cost incurred for its acquisition.

  Measurement and recognition criteria for income components.

  Following initial recognition, financial assets are measured at their fair value with any gains or losses resulting from a change in the fair value compared to the amortised cost recognised in a specific equity reserve recognised in the statement of comprehensive income up until said financial asset is derecognised or an impairment loss is recognised.
  Equity instruments, for which the choice has been made to classify them in this category, are measured at fair value

and the amounts recognised in other comprehensive income cannot be subsequently transferred to profit or loss, not even if they are sold (the so-called OCI exemption). The only component related to these equity instruments that is recognised through profit or loss is their dividends. Fair value is determined on the basis of the criteria already described for Financial assets measured at fair value through profit or loss.

For the equity instruments included in this category, which are not quoted on an active market, the cost approach is used as the estimate of fair value only on a residual basis and in a small number of circumstances, i.e., when all the measurement methods referred to above cannot be applied, or when there are a wide range of possible measurements of fair value, in which cost represents the most significant estimate.

Financial assets measured at fair value through other comprehensive income are subject to the verification of the significant increase in credit risk (impairment) required by IFRS 9, with the consequent recognition through profit or loss of an impairment loss to cover the expected losses.

- **Derecognition criteria**

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

Equity investments – accounting policies

- **Classification criteria**

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

- **Recognition criteria**

  Equity investments are recognised in the financial statements at purchase cost plus any related charges.

- **Measurement criteria**

  In the consolidated financial statements, equity investments in subsidiaries are consolidated using the full line-by-line method. Equity investments in associates and joint ventures are both measured at equity. At the end of each financial year or interim report date, an assessment is performed to determine if any objective evidence exists that an investment has been impaired. The recoverable value is then calculated taking into account the present value of the future cash flows that the investment will be able to generate, including the final disposal value of the investment. Any lower value, compared to the carrying amount, resulting from this calculation is charged to the income statement under "250 Gains (losses) on equity investments". The item also includes any future impairment gains where the reasons for the previous impairment losses no longer apply.

- **Derecognition criteria**

  Equity investments are derecognised from the financial statements when the contractual rights to cash flows deriving from the investment are lost or when the investment is transferred, with the substantial transfer of all related risks and rewards. Gains and losses on the sale of equity investments are charged to the income statement under the item "240 Gains (losses) on equity investments"; gains and losses on the sale of investments other than those measured at equity are charged to the income statement under the item "280 Gains (losses) on sales of investments".

QUANTITATIVE DISCLOSURE

(Amounts in thousands of Euro)

Type of exposure/amounts	Carrying amount			Fair value			Market value	Realised Gains/ Losses and impairment		Unrealised Gains/ Losses recognised in the Statement of Financial Position	
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3	Level 1	Gain	Loss	Gains (+)	Losses (-)
Financial assets measured at fair value through other comprehensive income	618		5,000	618		5,000					
Financial assets at fair value through profit or loss											
Equity investments			1,000			1,000					
Goodwill											

The value reported in Financial assets measured at fair value through other comprehensive income mainly includes the purchase for 200 stakes with a total value of € 5 million, accounting for 0.066% of the share capital of the Bank of Italy and the shares of Axactor Norway.

Equity investments amount to € 1,000 thousand and relate to Banca Sistema entering into an equal partnership with EBN Banco de Negocios S.A., taking a stake in the capital of EBNSISTEMA Finance S.L., and thereby entering the Spanish factoring market. Banca Sistema acquired an equity investment in EBNSISTEMA through a capital increase of € 1 million which gave Banca Sistema a 50% stake in the Madrid-based company.

SECTION 14 – EXPOSURE TO INTEREST RATE RISK ON POSITIONS NOT INCLUDED IN THE TRADING BOOK (ART. 448 CRR)

QUALITATIVE DISCLOSURE

The banking book consists of all the asset and liability-based financial instruments not included in the trading book. As already shown in this document, this risk on the positions included in the banking book consists of the possibility of negative changes in the cash flows or in the market value of Bank assets and liabilities due to adverse and unexpected movements of market rates.

Customer deposits on savings accounts and current accounts are at a fixed rate, as interbank funding transactions are predominantly at a fixed rate and with very short duration.

The interest rate risk connected with the funding transactions carried out by the Treasury Department is assumed in accordance with the policies and limits set by the Board of Directors.

Interest rate risk is monitored by identifying the most appropriate indicators for monitoring the changes in assets and liabilities with respect to the limits, investment and funding policies, and interest rate risk management policies, and any appropriate measures to ensure that the activity is carried out in accordance with the risk policies.

As at 31 December 2020, no interest rate risk hedging instruments were used.

QUANTITATIVE DISCLOSURE

In accordance with the guidelines given in Bank of Italy Circular no. 285/2013, which transposes the recommendations issued by the Basel Committee and the EBA Guidelines, the Internal Capital used to cover interest rate risk is calculated according to a simplified approach that breaks down the assets and liabilities in the banking book of Banks into 19 time buckets according to their residual lifetime. Variable-rate assets and liabilities are assigned to the various time buckets according to the interest rate repricing date.

Based on this model, assets and liabilities are entered in the payment schedule book in accordance with the criteria provided for in Bank of Italy Circular no. 272 "Manual for filling out the Accounts Matrix" and in Circular no. 115 "Instructions for filling out the supervisory reports of credit institutions on a consolidated basis", with the exception of:

- current accounts with positive balances, classified in the “On demand” bucket;
- overdraft accounts and demand deposits to be classified in accordance with the following instructions:
  - in the “On demand” bucket, by convention, a fixed share of 25% (the so-called “non-core component”) for retail counterparties and 50% for wholesale counterparties. Where it is not possible to distinguish between the two types of counterparty, the application of a single fixed share of at least 35% is recommended;
  - for the remaining amount (the so-called "core component") in the subsequent eight time buckets (from "up to 1 month" to "4-5 years"), in proportion to the number of months contained therein.

Furthermore, the Bank models its savings product “Conto Deposito” by considering the embedded option of early redemption. In particular, the historical percentage of recorded early redemptions is calculated for that item; said value is applied to the entire savings and deposits from the product and the relevant share is entered in the bucket at 1 day. The remaining sums are “bucketised” as a function of the contractual maturity chosen by the customer.

Within each time bucket, the asset and liability positions are multiplied by the weights derived from the product of a hypothetical change in rates and an approximation of the modified duration for each individual bucket.

Within each time bucket, the asset positions are offset against the liability positions, so as to obtain a net position.

To calculate the interest rate risk of the banking book, the Bank of Italy requires that when determining internal capital under normal conditions, the annual interest rate changes recorded over a 6-year observation period may be used as a reference, using the 1st percentile (decrease) or 99th percentile (increase) as an alternative and other shock scenarios chosen by the bank, based on the indications contained in subsection 4.4.3 "Interest rate shock scenarios for ongoing management" in EBA/GL/2018/02.To provide a more granular representation of the economic conditions of the banking book, rates of return between 0.5% and 5% can be used to differentiate the level of profitability of assets and liabilities.

With regard to the determination of internal capital under stressed conditions, institutions should assess the impact on economic value of a hypothetical change in rates of +/-200 basis points and the six EBA scenarios, considering the provisions of EBA GL 2018-02, while applying the EBA floor for negative shocks.

The table below shows the change in economic value under ordinary stress and the application of the six EBA scenarios (parallel and non-parallel scenarios) using the methodology set out in Annex C of Circular 285 and the related Internal Capital. The table below also indicates that the risk indicator (based on the Supervisory outlier test) is 3.7%, well below the regulatory limit of 20%.

Risk Management also calculates and monitors the exposure to interest rate risk in relation to changes in net interest income, which is lower than the change in economic value

(Amounts in thousands of Euro)

EXPOSURE TO INTEREST RATE RISK	AMOUNTS AT 31/12/2020
INTERNAL CAPITAL FOR INTEREST RATE RISK	7,702
OWN FUNDS	209,454
RISK INDICATOR	3.7
THRESHOLD LIMIT DEFINED BY THE REGULATION	20%

SECTION 15 – EXPOSURE TO SECURITISATION POSITIONS (ART. 449 CRR)

QUALITATIVE DISCLOSURE

The securitisation of loans and receivables is a financial technique that permits transformation of illiquid "assets" (loans and receivables, properties, other rights) into credit securities negotiable on the "bond" market. It is also a tool for funding and transferring risk.

Starting in 2016, Banca Sistema structured five securitisation transactions as originator and/or sponsor (while also acting as Master Servicer). These transactions are described as follows:

- Quinto Sistema Sec 2016 (redeemed in 2019), Quinto Sistema Sec 2017 (currently outstanding, rated, listed and whose senior securities are eligible as collateral for Eurosystem refinancing transactions) and Quinto Sistema Sec 2020. All three transactions involved loans and receivables portfolios deriving from salary- and pension-backed loans.
- Atlantis SPV: securitisation of factored receivables from debtors falling in the "public" category.
- BS IVA SPV: securitisation of factored VAT receivables.

Objectives of the Quinto Sistema Sec. transactions

The securitisation of salary- and pension-backed loans has the following objectives:

- Expansion of the sources of financing, by reaching investors "different" from those with which the Bank normally has relations, as institutional investors specialising in senior and mezzanine risk classes.
- Reduction of funding costs through the use of ABS as collateral for ECB loans and bilateral transactions.
- Taking advantage, where market conditions so allow, of opportunities to optimise regulatory capital: the creation of ABS securities (senior, mezzanine, and junior) allows, at higher and higher costs, the possibility of considering the sale of higher risk securities on the market, in compliance with the CRR, to realise the goal of freeing up the desired portion of any regulatory capital absorbed by the portfolio of salary-backed loans.
- Strategy of dynamic maintenance of balance between investments (Receivables deriving from salary-backed loans) and bank funding sources (specific funding). A typical characteristic of ABS securities is to be perfectly "self-repaying", with perfect matching between the duration of the investment and the duration of the funding, without any refinancing risk. Therefore, the duration contribution of the ABS is always proportionate to the duration of the securitised asset.

Atlantis Objectives

The Bank intended to benefit from certain characteristics of securitisation structures for loans and receivables deriving from the factoring business (particularly in terms of standardising the management process and potentially refinancing assets using dedicated transactions for each type of risk).

Obiettivi BS IVA SPV

The Bank has set up a platform that is entirely dedicated to the refinancing of VAT receivables. The securitisation makes Banca Sistema the direct assignee of the receivables from its customers, in addition to its role as Servicer pursuant to Law 130, as well as its role as Programme and Administration Agent (the entity in charge of implementing and coordinating the purchases by the SPV).

Securitisation risks

Securitisation risks refer to various types of risk that substantially relate to three specific roles/circumstances involving Banca Sistema:

- Investor in the ABS securities resulting from its own securitisation. When the portfolio is derecognised, and when certain securities continue to be recognised in the financial statements, the "ABS securities", and no longer the "loans and receivables", will have to be measured for financial reporting and prudential purposes;

- Servicer or other roles involved in the securitisation, with the natural Operational Risks that already existed before securitisation but which assume the nature of contractual and regulatory risks;
- Originator and/o Sponsor of the transaction. In addition to the foregoing, the Bank ultimately runs a reputational risk on the market in general, due to the greater transparency of the performance of the securitised portfolio (periodically analysed by rating agencies and investors) and the general performance of the securitisation.

The bank reports the securitised portfolios as loans in its statement of financial position and supervisory reports, as if the exposures had never been securitised.

The standardised approach is applied to these exposures.

The Bank does not hold third-party securitised exposures in its banking book.

ECAI

Per Quinto Sistema Sec 2017 (come era già avvenuto per la precedente operazione sugli attivi CQS/CQP Quinto Sisitema Sec 2016) le agenzie di Rating sono Moodys e DBRS in quanto: As previously done for the preceding transaction on the Quinto Sistema Sec 2016 salary- and pension-backed loan assets, the rating agencies for Quinto Sistema Sec 2017 are Moody's and DBRS insofar as:

- two ratings are needed to render the senior ABS securities eligible for refinancing operations with the ECB;
- they are the only two agencies that use an established method for rating a securitisation transaction involving salary-backed loans (other agencies, such as Fitch and S&P, while having a methodology, are not used by issuers for reasons related to cost and the conditioning of the "sovereign rating" on the rating that can be achieved for this type of transaction).

SECTION 16 – REMUNERATION POLICY
(ART. 450 CRR)

QUALITATIVE DISCLOSURE

The remuneration and incentive policies of the Banca Sistema Banking Group have been defined with the ultimate aim of achieving - in the interests of all stakeholders - remuneration systems that are consistent with the company's long-term goals, values and strategies, which are linked to company results and appropriately adjusted to take into account all risks assumed by the Group. In particular, the systems are to be consistent with the levels of capital and liquidity required to run the business to avoid incentive distortions of the type which encourage recipients to breach the provisions or expose the Group to take on excessive risks.

QUANTITATIVE DISCLOSURE

The following disclosure relates to the remuneration paid by the Group during 2020, for both the fixed and the variable component, for the different categories of recipients. For further details, please refer to the document "Report_on_ Remuneration_2021", available on the bank's website www.bancasistema.it.

TABLE – Fees paid to members of the management and control bodies and to general managers and other key management personnel.

(A)	(B)	(C)	(D)		(1)					(2)	(3)		(4)	(5)	(6)	(7)	(8)
Name and surname	Position held	Time in position	Expiry of office	Notes	Fixed remuneration					Committee membership fees	Non-equity variable remuneration		Non-cash benefits	Other remu-nera-tion	Total	Fair Value of equity remunera-tion	Severance indemnity or employment termination compensation
					Fixed remune-ration	Offices held pursuant to art. 2389, par. 3 of the Civil Code	Attendan-ce fee	Capped reimbur-sement of expenses	Fixed remu-neration of employees		Bonuses and other incentives	Profit sharing					
Garbi Gianluca	Chief Executive Officer	From 01/01/2020	Approval of finan. statements 31/12/2020		265				589		301.20		50		1,205.20		
Luitgard Spögler	Chairperson Of Bod	From 01/01/2020	Approval of finan. statements 31/12/2020		150		27								177		
Giovanni Antonino Puglisi	Director	From 01/01/2020	Approval of finan. statements 31/12/2020		30		8.50			10					48.5		
Daniele Pittatore	Director	From 01/01/2020	Approval of finan. statements 31/12/2020		30		9			30					69		
Carlotta De Franceschi	Director	From 01/01/2020	Approval of finan. statements 31/12/2020		30		9			20					59		
Laura Ciambellotti	Director	From 01/01/2020	Approval of finan. statements 31/12/2020		30		9			15					54		
Federico Ferro Luzzi	Director	From 01/01/2020	Approval of finan. statements 31/12/2020		30		9			25					64		
Francesco Galietti	Director	From 01/01/2020	Approval of finan. statements 31/12/2020		30		9			5					44		
Marco Giovannini	Director	From 01/01/2020	Approval of finan. statements 31/12/2020		30		8			10					48		
Massimo Conigliaro	Chairperson of Board of Stat. Auditors	From 01/01/2020	Approval of finan. statements 31/12/2020		46.66					15					61.66		
Biagio Verde	Standing Auditor	From 01/01/2020 to 23/04/2020			8										8		
Marziano Viozzi	Standing Auditor	From 24/04/2020	Approval of finan. statements 31/12/2020		23.33										23.33		
Lucia Abati	Standing Auditor	From 01/01/2020	Approval of finan. statements 31/12/2020		31.33										31.33		
I) fees in the firm that prepares the financial statements					**734.33**		**88.5**		**589**	**130**	**301.20**		**50**		**1,893**		
Garbi Gianluca	Chairperson of BoD of ProntoPegno	From 12/10/2018	31/12/2021		16.95												
Lucia Abati	Chairperson of Board of Statutory Auditors of ProntoPegno	From 12/10/2018	31/12/2021		12.97												
II) fees from subsidiaries and associates					**29.92**										**29.92**		
III) Total					**764.25**		**88.5**			**130**	**301.20**		**50**		**1,923**		

Table: Aggregate Quantitative Information on remuneration, broken down by "key personnel" category.

ANNEX UNDER ART. 450 CRR, letter h) AGGREGATE QUANTITATIVE INFORMATION ON REMUNERATION, BROKEN DOWN BY "KEY PERSONNEL" CATEGORY indicating:

- **i)** **remuneration amounts for the financial year, divided into fixed and variable remuneration and number of beneficiaries;**
- **ii)** **amounts and forms for the variable remuneration component, divided into cash, shares, share-linked instruments and other types;**
- **iii)** **amounts of outstanding deferred remuneration, divided into awarded and unawarded portions;**
- **iv)** **amounts of deferred remuneration granted during the financial year, paid out and reduced through performance adjustments;**
- **v)** **new sign-on and severance payments made during the financial year, and number of beneficiaries;**
- **vi)** **amounts of severance payments granted during the financial year, number of beneficiaries and the highest amount granted per person.**

		i) remuneration			ii) amounts and forms of the variable component				iii) deferred remuneration		iv) deferred remuneration			v) sign-on and severance payments				vi) post-employment benefits (TFR)		
Company	No. of beneficiares	Fixed	Variable remuneration paid in 2020(1)	Total	Variable remuneration to be paid in 2021(2)	Shares(3)	Share-linked instruments	Other types	Awarded(4)	Unawarded(5)	Granted	Paid	Reduced	Sign-on	No. of beneficiares	Severance	No. of beneficiares	Granted	No. of beneficiares	Highest amount
A) KEY MANAGERS																				
Banca Sistema SpA	1	904,000	301,200	1,205,200	369,524	369,524			282,800	785,098								146,990	1,00	146,990
B) SENIOR MANAGERS IN CHARGE OF THE MAIN BUSINESS LINES OR CORPORATE FUNCTIONS, REPORTING DIRECTLY TO THE CEO, GENERAL MANAGER OR CO-GENERAL MANAGERS																				
Banca Sistema SpA	10	1,942,608	216,250	2,158,858	261,500	513,500			127,500	207,900								13,400	1,00	13,400
C) SENIOR AND HIGHER-LEVEL MIDDLE MANAGERS IN CHARGE OF CONTROL FUNCTIONS																				
Banca Sistema SpA	5	886,908	125,000	1,011,908	101,500				47,500											
D) OTHER RISK TAKERS																				
Banca Sistema SpA	9	1,251,498	155,750	1,407,248	117,000	15,000			22,500											
E) KEY MANAGERS OPERATING WITHIN THE BANK'S DISTRIBUTION NETWORKS																				
Banca Sistema SpA	2	328,26	24,000	352,262	40,000	25,000			10,000	27,000										
Banca Sistema SpA	**27**	**5,313,276**	**822,200**	**6,135,476**	**889,524**	**923,024**			**490.380,00**	**1,019,998**										

(1) **variable remuneration paid in 2020: upfront 2019 bonus + deferred portion of 2016 bonus**
for A) KEY MANAGERS: 301,200.00 = 282,300 upfront 2019 bonus + 18,900 deferred portion of 2016 bonus

(2) **variable remuneration to be paid in 2021: upfront 2020 bonus + deferred portion of 2017**
for A) KEY MANAGERS: 369,523.5 = 306,524 upfront 2020 bonus + 63,000 deferred portion of 2017 bonus to be paid in 2021

(3) **shares: value of shares to distribute in 2021**
for A) KEY MANAGERS: 369,524 = 306,524 upfront 2020 bonus + 63,000 deferred portion of 2017 bonus

(4) **awarded: deferred portion of 2018 bonus**
for A) KEY MANAGERS: 282,800: deferred portion for 2018

(5) **unawarded: deferred portion of 2019 and 2020 bonus**
for A) KEY MANAGERS: 785,098.00 = deferred portion of 2019 bonus payable in 2023 and 2020 bonus payable in 2024

SECTION 17 – LEVERAGE
(ART. 451 CRR)

QUALITATIVE DISCLOSURE

Starting from 1 January 2015, the Leverage Ratio was introduced with the objective of containing the degree of Banks' debt entering a minimum level to hedge overall exposures by means of own funds. The minimum level of the ratio was set at 3% by the Basel Committee.

The Leverage Ratio is calculated as the ratio between the Tier 1 Capital and the overall exposure. In particular, the denominator of the ratio consists of the total adjusted exposures, excluding the assets deducted from Tier 1 Capital, and including the off-statement of financial position exposures.

Instead, in reference to the numerator, during the period from 1 January 2015 to 31 December 2021 the Leverage Ratio is calculated by using:

- the "transitional" Tier 1 Capital, i.e. the sum of the Common Equity Tier 1 (CET1) Capital and Additional Tier 1 (AT1) Capital of the bank calculated according to the applicable rules;
- the "full phase-in" Tier 1 Capital, i.e. stripped of the exemptions pursuant to the Transitional provisions.

As at 31 December 2020, a leverage ratio equal to 4.72%, above the minimum regulatory level proposed by the Basel Committee, was recorded. The ratio is currently reported quarterly to the Bank of Italy for monitoring purposes.

The bank considers its leverage risk to be low, partly given that about 23% of the total assets used to calculate the ratio consists of the treasury portfolio that is wholly comprised of Italian Government Securities having an overall duration of less than two years. The short duration of the portfolio guarantees both limited changes in the fair value of the securities and, in the event of significant negative changes in fair value, the possibility of deciding whether to keep the security until maturity, de facto cancelling any losses that might be realised.

QUANTITATIVE DISCLOSURE

(Amounts in thousands of Euro)

Leverage	31.12.2020
Total assets	3,625,044
SFTs: Exposure in accordance with Article 429 (5) and 429 (8) of the CRR	5,545
Items deducted from Own Funds - Full phase-in	-33,242
Items deducted from Own Funds - Transitional	-33,242
Repurchase agreement add-ons	6
Derivatives: Add-on	
Off-balance sheet items	82,163
(-) Exposures exempted in accordance with Article 429 (14) of the CRR	-40.378
Total exposure of the Leverage Ratio - Full phase-in	3,639,139
Total exposure of the Leverage Ratio - Transitional	3,639,139
Tier 1 capital - fully phased-in definition	171,797
Tier 1 capital - transitional definition	171,797
Leverage - Full phase-in	4.72%
Leverage - Transitional	4.72%

SECTION 19 – USE OF CREDIT RISK MITIGATION TECHNIQUES (ART. 453 CRR)

QUALITATIVE DISCLOSURE

The strategies pursued by the Banking Group require that credit lines be preferably backed by appropriate guarantees and instruments to mitigate risk. Given their capacity to spread credit risk, when managed in conjunction with customer knowledge, guarantees become the primary and most effective instrument for effectively mitigating risk. The Banca Sistema Group has implemented the requirements set forth in Regulation (EU) 575/2013 for the purposes of recognising the effects of mitigating credit risk due to collateral and personal guarantees in place for credit protection.

Lending to SMEs is contingent upon the presence of the guarantee issued by the National Guarantee Fund (the average guarantee of outstanding loans at 31 December is about 80%) for SMEs (Italian Law no. 662/96 as amended) managed by Mediocredito Centrale S.p.A. (MCC). The Bank has decided to discontinue lending to SMEs, limiting itself to managing this portfolio exclusively as run-off, and has entrusted monitoring to the Central Credit Department.

These exposures fall in the regulatory segments "Retail Exposures" and "Exposures to companies".

Lastly, the category of personal financing which allows an advance to be obtained from the sums deposited on the term deposit converges in particular in the "Retail exposures" segment. The loan granted is guaranteed by the encumbered sums.

Moreover, as at 31 December 2020, transactions of "credit lines opening on a current account secured by collateral" were granted for an amount equal to approximately € 77.7 million. The value of the exposure is backed by eligible collateral for the purpose of credit risk mitigation[7].

In regard to the exposures deriving from the salary- and pension-backed loans, the Bank recognises the life insurance policies taken out in favour of the lending institution as a means of reducing the credit risk (after the assignment, the Bank becomes the beneficiary of the policies), provided that those policies meet the conditions specifically indicated in Regulation (EU) 575/13, Art. 212 – Requirements for other funded credit protection, paragraph 2.

To be able to use the unfunded credit protection, the Bank identifies the life insurance policies that it intends to use to replace the weighting ratio of the guarantor with the ratio of the guaranteed party, while verifying that the insurance company is authorised to offer insurance and that it has an ECAI credit rating.

(7) Regulation (EU) 575/2013 Title II, Chapter 4.

QUANTITATIVE DISCLOSURE

(Amounts in thousands of Euro)

Segment	On-statement of financial position exposure	Off-statement of financial position exposure	Post CRM on-statement of financial position exposure	Post CRM off-statement of financial position exposure	RWA*
Central authorities and central banks	1,364,844		1,428,579		19,809
Territorial Entities	347,713		347,713		68,840
Public Sector Institutions	252,375	220,630	252,375	44,122	68,898
Supervised brokers	76,502	321,727	76,502	2,111	18,226
Companies and other parties	326,353	121,897	316,176	6,029	251,743
Retail	998,684	20,048	864,493	42	337,151
Exposures secured by properties	1,512		1,512		529
Non-performing exposures	199,553	10,389	197,635	650	287,175
Exposures in equity instruments	6,618		6,618		6,618
Other exposures	58,089	5,641	58,089	5,641	61,163
Total	3,632,243	700,331	3,549,692	58,595	1,120,152

(*) RWA is gross of the contribution to the default fund of the Compensation and Guarantee Fund, contrary to what is reported in section 4 "Risk-weighted assets - credit and counterparty risk".

SECTION 22 - DISCLOSURE OF NON-PERFORMING AND FORBORNE EXPOSURES (EBA/GL/2018/10)

QUALITATIVE DISCLOSURE

This section contains the disclosure of non-performing and forborne exposures pursuant to the EBA/GL/2018/10 guidelines.

QUANTITATIVE DISCLOSURE

Table 1: Credit quality of forborne exposures

(Amounts in thousands of Euro)

		Gross carrying amount/nominal amount of forborne exposures				Accumulated impairment, accumulated negative changes in fair value due to credit risk and allowances		Collateral received and financial guarantees received on forborne exposures	
		Performing forborne exposures	Non-performing forborne exposures			On performing forborne exposures	On non-performing forborne exposures		Of which collateral and financial guarantees received on non-performing forborne exposures
				Of which defaulted	Of which impaired				
1	**Loans and advances**	**1,062**	**664**	**664**	**664**	**-7**	**-487**	**177**	**177**
2	Central Banks								
3	Public administrations								
4	Credit institutions								
5	Other financial companies								
6	Non-financial companies	1,062	664	664	664	-7	-487	177	177
7	Households								
8	**Debt instruments**								
9	**Loan commitments given**								
10	**Total**	**1,062**	**664**	**664**	**644**	**-7**	**-487**	**177**	**177**

Table 2: Credit quality of non-performing and performing exposures by days past due

(Amounts in thousands of Euro)

		Gross amount											
		Performing exposures			Non-performing exposures								
			Not past due or Past due ≤ 30 days	Past due > 30 days ≤ 90 days		Unlikely to pay that are not past due or past due ≤ 90 days	Past due > 90 days ≤ 180 days	Past due > 180 days ≤ 1 year	Past due > 1 year ≤ 2 years	Past due > 2 years ≤ 5 years	Past due > 5 years ≤ 7 years	Past due > 7 years	Of which: defaulted
1	**Loans and advances**	**2,414,933**	**2,070,330**	**344,602**	**251,164**	**32,203**	**3,860**	**7,948**	**16,840**	**134,342**	**27,700**	**28,270**	**251,164**
2	Central Banks	6	6										
3	Public administrations	1,034,778	697,105	337,672	150,873	12,657	1,317	3,594	10,090	81,819	17,579	23,817	150,873
4	Credit institutions	10,302	10,302										
5	Other financial companies	52,354	52,353	1	7	2	1		2	1			7
6	Non-financial companies	287,483	285,005	2,478	86,940	16,769	793	1,559	4,123	50,496	8,747	4,453	86,940
7	Of which: SMEs	90,849	90,847	3	7,639	1,404	16	35	3,313	2,871			7,639
8	Households	1,030,010	1,025,559	4,451	13,344	2,775	1,749	2,795	2,625	2,026	1,374		13,344
9	**Debt instruments**	**873,637**	**873,637**										
10	Central Banks												
11	Public administrations	873,637	873,637										
12	Credit institutions												
13	Other financial companies												
14	Non-financial companies												
15	**Off-statement of financial position**	**447,050**			**10,389**								**10,389**
16	Central Banks												
17	Public administrations	220,630			3,250								3,250
18	Credit institutions												
19	Other financial companies	106,767											
20	Non-financial companies	117,039			7,139								7,139
21	Households	2,614											
22	**Total**	**3,735,620**	**2,943,967**	**344,602**	**261,553**	**32,203**	**3,860**	**7,948**	**16,840**	**134,342**	**27,700**	**22,630**	**261,553**

Table 3: Performing and non-performing exposures and related allowances

(Amounts in thousands of Euro)

		Gross carrying amount/nominal amount						Accumulated impairment, accumulated negative changes in fair value due to credit risk and allowances						Cumulative partial write-offs	Collateral and financial guarantees received	
		Performing			Non-performing			Performing exposures – accumulated impairment and allowances			Non-performing exposures – accumulated impairment, accumulated negative changes in fair value due to credit risk and allowances				on performing exposures	on non-performing exposures
			Of which Stage 1	Of which Stage 2		Of which Stage 2	Of which Stage 3		Of which Stage 1	Of which Stage 2		Of which Stage 2	Of which Stage 3			
1	**Loans and advances**	**2,414,933**	**2,280,738**	**134,194**	**245,523**		**251,161**	**-7,334**	**6,553**	**-780**	**-46,028**		**-46,028**		**1,033,839**	**16,305**
2	Central Banks	6	6					-0.003	-0.003							
3	Public administrations	1,034,778	1,014,456	20,322	145,232		150,873	-3,693	-3,522	-171	-8,591		-8,591			
4	Credit institutions	10,302	10,301	0.43				-18.8	-18.81	-0.003						
5	Other financial companies	52,354	52,354		7		3.76	-38.1	-38.1		-0.036		-0.036		20,893	
6	Non-financial companies	287,483	264,686	22,797	86,940		86,940	-1,768	-1,623	-145	-34,605		-34,605		100,233	8,425
7	Of which: SMEs	90,849	85,685	5,164	7,639		7,639	-495	-460	-35	-1,766		-1,766		59,418	271
8	Households	1,030,010	938,935	91,074	13,344		13,344	-1,816	-1,351	-464	-2,832		-2,832		912,713	7,880
9	**Debt instruments**	**448,082**	**448,082**					**-218**	**-218**							
10	Central Banks															
11	Public administrations	448,082	448,082					-218	-218							
12	Credit institutions															
13	Other financial companies															
14	Non-financial companies															
15	**Off-statement of financial position**	**442,773**	**418,007**	**24,766**	**10,389**		**10,389**	**26**	**26**						**23,236**	**452**
16	Central Banks															
17	Public administrations	220,610	220,610		3,250		3,250	0.001	0.001						20	
18	Credit institutions							0.09	0.09							
19	Other financial companies	106,767	106,767												361	
20	Non-financial companies	112,879	88,342	24,537	7,139		7,139	26	26						22,601	452
21	Households	2,517	2,288	229				0.06	0.06						254	
22	**Total**	**3,305,788**	**3,146,827**	**158,960**	**255,912**		**261,550**	**-7,526**	**6,361**	**-780**	**-46,028**		**-46,028**		**1,057,075**	**16,757**

SECTION 23 - REPORTING AND DISCLOSURE OF EXPOSURES SUBJECT TO MEASURES APPLIED IN RESPONSE TO THE COVID-19 CRISIS (EBA/GL/2020/07)

QUALITATIVE DISCLOSURE

By means of a communication dated 30 June 2020, the Bank of Italy implemented the EBA Guidelines on reporting and disclosure of exposures subject to measures applied in response to the COVID-19 crisis (EBA/GL/2020/07). The purpose of the guidelines is to monitor, on a European level and in a harmonised manner, the moratoria granted to support customers in response to the COVID-19 crisis as well as to provide an accurate understanding of the risk profile of the supervised institutions, consistent with FINREP consolidated reporting information. To this end, institutions are required to disclose information on:

- exposures subject to legislative and non-legislative moratoria applied in light of the COVID-19 crisis (EBA/GL/2020/02);
- exposures subject to forbearance measures applied in response to the COVID-19 crisis;
- new exposures covered by public guarantee schemes introduced in Member States.

QUANTITATIVE DISCLOSURE

Table 4: Disclosure of loans and advances subject to legislative and non-legislative moratoria

	Gross carrying amount				
		Performing			
			Of which grace period on principal and interest	Of which: forborne exposures	Of which: instruments with a significant increase in credit risk after initial recognition but which are performing (Stage 2)
Loans and advances subject to moratoria	**12,200,608**	**6,304,500**	**6,032,019**		**2,507,349**
of which: to households					
of which: secured by residential real estate put up as collateral					
of which: to non-financial companies	12,200,608	6,304,500	6,032,019		2,507,349
of which: to SMEs	3,903,104	3,895,559	3,895,559		2,507,349
of which: secured by non-residential real estate put up as collateral					

	Gross carrying amount			
	Non-performing			
		Of which grace period on principal and interest	Of which: forborne exposures	Of which: unlikely to pay that are not past due or are past due less than 90 days
Loans and advances subject to moratoria	**5,896,108**	**5,896,108**		
of which: to households				
of which: secured by residential real estate put up as collateral				
of which: to non-financial companies	5,896,108	5,896,108		
of which: to SMEs	7,545	7,545		
of which: secured by non-residential real estate put up as collateral				

	Accumulated impairment and accumulated negative changes in fair value due to credit risk				
		Performing			
			Of which grace period on principal and interest	Of which: forborne exposures	Of which: instruments with a significant increase in credit risk after initial recognition but which are performing (Stage 2)
Loans and advances subject to moratoria	**-958,615**	**-107,942**	**-104,723**		**-8,909**
of which: to households					
of which: secured by residential real estate put up as collateral					
of which: to non-financial companies	-958,615	-107,942	-104,723		-8,909
of which: to SMEs	-36,388	-36,145	-36,145		-8,909
of which: secured by non-residential real estate put up as collateral					

	Accumulated impairment and accumulated negative changes in fair value due to credit risk				Gross carrying amount
	Non-performing				Flows into non-performing exposures
		Of which grace period on principal and interest	Of which: forborne exposures	Of which: unlikely to pay that are not past due or are past due less than 90 days	
Loans and advances subject to moratoria	**-850,673**	**-850,673**			
of which: to households					
of which: secured by residential real estate put up as collateral					
of which: to non-financial companies	-850,673	-850,673			
of which: to SMEs	-243	-243			
of which: secured by non-residential real estate put up as collateral					

Table 5: Breakdown of loans and advances subject to legislative and non-legislative moratoria by remaining duration of moratoria

	Number of debtors		Gross amount				Remaining duration of moratoria					
		of which granted		of which granted			≤ 3 months	> 3 months ≤ 6 months	> 6 months ≤ 9 months	> 9 months ≤ 12 months	> 12 months ≤ 18 months	> 18 months
					Of which: legislative moratoria	of which past due						
Loans and advances subject to moratoria	**41**	**41**	**12,200,608**	**12,200,608**	**12,200,608**				**12,200,608**			
of which: to households												
of which: secured by residential real estate put up as collateral												
of which: to non-financial companies				12,200,608	12,200,608				12,200,608			
of which: to SMEs				3,903,104	3,903,104				3,903,104			
of which: secured by non-residential real estate put up as collateral												

Table 6: Information on new loans and advances subject to newly implemented public guarantee schemes introduced in response to the COVID-19 crisis

	Gross amount		Maximum amount of the guarantee that can be considered	Gross carrying amount
		of which: subject to forbearance measures	Public guarantees received	Flows into non-performing exposures
New loans and advances subject to public guarantee schemes	**65,491,867**			
of which: to households				
of which: secured by residential real estate put up as collateral				
of which: to non-financial companies	65,491,867			
of which: to SMEs	30,172,240			
of which: secured by non-residential real estate put up as collateral				

COUNTRY-BY-COUNTRY REPORTING

The 4th update of Bank of Italy Circular no. 285/2013, under Title III, Chapter 2, transposes the rules on country-by-country reporting, introduced by Article 89 of Directive 2013/36/EU ("CRD IV"), into Italian law. In line with this provision, the Bank is required to disclose annually qualitative and quantitative information, as an annex to the financial statements or on its website. For this reason, the information indicated in letters a), b) and c) of Annex A to Part One, Title III, Chapter 2, with reference to the situation at 31 December 2020, needs to be disclosed.

In detail:

a. Name of the company and nature of its activities;

b. Turnover;

c. Number of employees on a full-time equivalent basis;

d. Profit or loss before tax;

e. Tax on profit or loss;

f. Public subsidies received.

Banca Sistema only operates in Italy. Therefore, the information required by the regulations set out in the table below only applies to Italy.

The required information is provided below

a) Name of the company and nature of its activities

The Banca Sistema Group operates in Italy and is composed of the following companies:

- Banca Sistema S.p.A. - Parent of the Banca Sistema Group - Banking
- Specialty Finance Trust Holdings Limited – Vehicle - Based in London
- Largo Augusto Servizi e Sviluppo S.r.l. - Vehicle
- ProntoPegno S.p.A - Banking
- EBNSistema Finance S.l.u. - Spanish joint venture

b) Turnover

The turnover of a bank is the "total income" reported in "item 120" of the income statement. Therefore, the turnover reported by the Banca Sistema Group at 31 December 2020 was: **€ 101,494 thousand**.

c) Number of employees on a full-time equivalent basis

This section illustrates the ratio between the total number of hours worked in 2020 by all employees of the Banca Sistema Group, excluding overtime, and the total number of hours per year under the national collective bargaining agreement for a full-time employee.

Total hours worked in 2020/Total hours per year under the national collective bargaining agreement (CCNL) for a full-time employee.

In 2020, the number of employees calculated on this basis was 228.

d) Profit or loss before tax

"Profit or loss before tax" refers to item 290 of the income statement under Circular no. 262.

Pre-tax profit from continuing operations: **€ 36,302 thousand**.

e) Tax on profit or loss

"Tax on profit or loss" refers to item 300 of the income statement under Circular no. 262 and Income taxes: **€ (11,009) thousand**.

f) Public subsidies received

"Public subsidies received" includes subsidies received directly from public administrations. This item does not include transactions executed by central banks for financial stability purposes or transactions aimed at facilitating the transmission mechanism of monetary policy. Similarly, transactions that fall under the state aid schemes approved by the European Commission have not been considered. Public subsidies received: the Group did not receive any public subsidies during 2020.

STATEMENT OF THE MANAGER IN CHARGE OF FINANCIAL REPORTING

The Manager in charge of financial reporting, Alexander Muz, hereby declares that, pursuant to Art. 154-bis, paragraph 2, of the Consolidated Law on Finance, the accounting information contained in this “Disclosure by Institutions pursuant to Regulation (EU) no. 575/2013 – 31 December 2020” corresponds to the company's documents, books and accounting records.

Alexander Muz
Manager in charge
of financial reporting

GLOSSARY

The definitions of the main technical terms used in the document are provided below.

Categories of financial instruments provided for by IAS 39
Trading assets, which include the assets acquired to be sold in the short term, or also belonging to instrument portfolios managed on a single basis in order to realise profits in the short term; assets measured at fair value, for which the IAS allow the assets which the entity nevertheless decides to recognise at fair value to be classified in that category with the change in value recognised in the income statement in compliance with certain case studies provided for by IAS 39; held-to-maturity investments, non-derivative financial assets with established maturity date and fixed or determinable payment schedule for which the actual intention and ability to hold them to maturity exists; loans and receivables, non-derivative assets with fixed or determinable payments, not quoted in an active market; available-for-sale financial assets.

CET1
Common Equity Tier 1 capital.

Common equity tier 1 ratio (CET1 Ratio)
This is the ratio between Common equity tier 1 (CET1) capital and total risk-weighted assets.

CRM
Credit Risk Mitigation.

Default
The declared inability to honour one's own debts and/or payment of interest thereon.

IAS/IFRS
The IAS (International Accounting Standards) are issued by the International Accounting Standards Board (IASB). The standards issued after July 2002 are named IFRS (International Financial Reporting Standards).

IASB (International Accounting Standard Board)
The IASB (in the past, named IASC) is responsible for issuing the IAS/IFRS.

ICAAP
The regulation of "Pillar 2" requires that banks implement the processes and instruments of the Internal Capital Adequacy Assessment Process (ICAAP) to determine the internal capital levels sufficient to cope with any type of risk, even those not covered by the overall minimum capital requirement ("Pillar 1"), within the scope of an assessment of the current and foreseeable exposure which takes into account the strategies and the developments in the economic and business environment.

Impairment
With reference to a financial asset, a situation of impairment occurs when the carrying amount of said asset is greater than the estimate of its recoverable amount.

Leverage Ratio
In the banking sector, leverage is generally defined as the ratio between the net equity of the bank and its total assets.

Non performing
A term generally referring to irregular loans.

Probability of Default (PD)
This represents the probability that the debtor will default over a one-year time horizon.

Rating
An evaluation of a company's quality or of its debt-security issues based on the financial soundness and outlook of the company.
Said evaluation is performed by specialised agencies or by the bank based on internal models.

Credit risk
This represents the risk that an unexpected change of the creditworthiness of a counterparty, of the guarantees thereby provided, or even the margins thereby used in case of insolvency, may generate an unexpected change in the bank's credit quality.

Market risk
Risks deriving from fluctuations in the value of the financial instruments traded on the market (shares, bonds, derivatives, securities denominated in foreign currency) and of financial instruments whose value is connected with market variables (loans to customers as regards the interest rate component, deposits in euro and in foreign currency, etc.).

Liquidity risk
The possibility that the entity is unable to meet its own payment obligations due to its inability to liquidate assets or obtain adequate funding from the market (funding liquidity risk) or due to the difficulty/impossibility of easily converting financial assets into cash without significantly and negatively affecting their price due to insufficient depth of the financial market or temporary market disruptions (market liquidity risk).

Operational risk
Operational risk is the risk of loss arising from inadequate or non-functioning processes, human resources or systems, or from external events. Operational risk includes legal risk, i.e. the risk of losses deriving from statutory or regulatory violations, from contractual or non-contractual liability, or from other disputes, ICT risk (Information and Communication Technology), and model risk. Strategic and reputational risks are not included.

Risk Management
Activity of acquiring, measuring, assessing, and globally managing the various types of risk and their hedging.

RWA (Risk Weighted Assets)
On- and off-statement of financial position assets (derivatives and guarantees) that are classified and weighted according to different ratios tied to the risks, pursuant to the banking regulations issued by regulatory bodies to calculate the solvency ratios.

GLOSSARY

The definitions of the main technical terms used in the document are provided below.

Tier 1
Tier 1 capital includes the Common Equity Tier 1 capital (CET1) and the Additional Tier 1 capital (AT1).

Tier 1 ratio
This is the ratio between Tier 1 Capital, which includes the Common Equity Tier 1 Capital (CET1) and the Additional Tier 1 Capital (AT1), and the total of risk-weighted assets.

Tier 2
Tier 2 Capital is largely composed of eligible subordinated liabilities.

Total capital ratio
Capital ratio referring to the sum of constituent components of Own Funds (Tier 1 and Tier 2).