AO Toyota Bank

Financial Statements
for 2017
and Independent Auditors' Report

CONTENTS

Independent Auditors' Report

To the Shareholders and Supervisory Board of AO Toyota Bank

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of AO Toyota Bank (the "Bank"), which comprise the statement of financial position as at 31 December 2017, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

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

Basis for Opinion

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

Audited entity: AO Toyota Bank

Registration No. in the Unified State Register of Legal Entities 1077711000058 on 3 April 2007.

Moscow, Russian Federation

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

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

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

Key Audit Matters

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

Impairment allowance for retail loans

Please refer to the Note 13 in the financial statements.

The key audit matter	How the matter was addressed in our audit
The Bank estimates impairment allowance for retail loans using professional judgment and subjective assumptions. Due to the significant volume of retail loans (comprising 78% of total assets) and the related estimation uncertainty, this area is a key audit matter. We focused on the analysis of adequacy of collective impairment allowance for retail loans in comparison with the historical losses. We also analysed key assumptions and judgements used by the Bank for calculation of impairment allowance.	In respect of impairment allowance for retail loans, calculated using the statistical models, we tested the estimation principles and their implementation, as well as the input data. - We reviewed accuracy of calculation of historical losses and compared main assumptions with our own assessment in relation to key input data. - We tested reports on calculation of impairment allowance, produced by the Bank's systems, for completeness and accuracy of input data and reviewed calculations accuracy of these reports. We also assessed whether the financial statements disclosures appropriately reflect the Bank's exposure to credit risk.

Impairment allowance for loans to auto dealers	
Please refer to the Note 13 in the financial statements.	
The key audit matter	**How the matter was addressed in our audit**
The Bank estimates impairment allowance for loans to auto dealers using professional judgment and subjective assumptions. Due to the significant volume of loans to auto dealers (comprising 13% of total assets) and uncertainty inherent to their measurement, this area is a key audit matter. We focused on the most significant loans and analysed the adequacy of collective impairment allowance for loans to auto dealers.	We assessed the design and operating effectiveness of the controls related to assignment of borrower's internal risk-rating. For a sample of loans, for which a potential changes in impairment allowance may have a significant impact on Bank's performance and financial statements, we assessed the accuracy of assigned borrower's internal risk-rating and the adequacy of the amount of recognized impairment allowance by means of an analysis of financial and non-financial information provided to us. For loans that were subject to an individual impairment assessment we analysed assumptions used by the Bank for calculation of expected future cash flows, including cash flows from operating activities and the value of realizable collateral, based on our own relevant industry understanding and other available market information. We also assessed whether the financial statements disclosures appropriately reflect the Bank's exposure to credit risk.

Other Information

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

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

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

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

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

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

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

Auditors' Responsibilities for the Audit of the Financial Statements

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

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

— Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

— Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.

— Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

— Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

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

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

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

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

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

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

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

— the Bank's compliance with mandatory ratios as at 1 January 2018 established by the Bank of Russia; and

— whether the elements of the Bank's internal control and organization of its risk management systems comply with the requirements established by the Bank of Russia.

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

Our findings from the procedures performed are reported below.

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

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

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

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

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

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

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

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

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

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

Shevarenkov Evgeny Victorovich
JSC "KPMG"
Moscow, Russian Federation

28 April 2018

(expressed in thousands of Russian Roubles)

	Notes	2017	2016
Interest income	4	6 836 670	6 674 433
Interest expense	4	(4 009 169)	(3 826 070)
Net interest income		**2 827 501**	**2 848 363**
Fee and commission income	5	109 627	410 594
Fee and commission expense	5	(117 249)	(332 464)
Net fee and commission (expense) income		**(7 622)**	**78 130**
Net foreign exchange expense	6	(138)	(178)
Other operating income	7	197 386	111 484
Operating income		**3 017 127**	**3 037 799**
Charge for impairment losses	13	(238 329)	(238 631)
Personnel expenses	8	(557 535)	(514 720)
Provision under buy-back program	19	(364)	6 561
Other general and administrative expenses	9	(996 256)	(871 829)
Profit before income tax		**1 224 643**	**1 419 180**
Income tax expense	10	(265 657)	(302 077)
Profit and total comprehensive income for the year		**958 986**	**1 117 103**

The financial statements were approved by the Management Board on 28 April 2018.

Koloshenko A.V.
President

Zvereva E.V.
Deputy Chief Accountant

The statement of profit or loss and other comprehensive income is to be read in conjunction with the notes to, and forming part of, the financial statements.

(expressed in thousands of Russian Roubles)

	Notes	2017	2016
ASSETS			
Cash and cash equivalents	11	1 202 696	756 306
Mandatory reserve deposit with the Bank of Russia	11	238 908	13 303
Loans to banks	12	3 343 251	3 400 836
Loans to customers	13	51 578 465	47 945 612
Property, equipment and intangible assets	14	264 801	223 448
Current tax asset	10	25 328	51 005
Other assets	15	150 565	176 121
Total assets		**56 804 014**	**52 566 631**
LIABILITIES			
Loans from banks	16	19 957 380	18 017 703
Other borrowings and customers' accounts	17	15 520 032	19 269 146
Bonds issued	18	8 123 028	3 094 886
Subordinated borrowings	18	1 414 555	1 414 393
Deferred tax liability	10	140 027	141 977
Other liabilities	19	322 185	260 705
Total liabilities		**45 477 207**	**42 198 810**
EQUITY			
Share capital	20	5 440 000	5 440 000
Additional paid-in capital		1 343 400	1 343 400
Retained earnings		4 543 407	3 584 421
Total equity		**11 326 807**	**10 367 821**
Total liabilities and equity		**56 804 014**	**52 566 631**

Koloshenko A.V.
President

Zvereva E.V.
Deputy Chief Accountant

The statement of financial position is to be read in conjunction with the notes to, and forming part of, the financial statements.

(expressed in thousands of Russian Roubles)

	Notes	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES			
Interest receipts		6 638 809	6 661 225
Interest payments		(3 982 520)	(3 733 300)
Fee and commission receipts		107 247	403 960
Fee and commission payments		(114 870)	(323 359)
Net receipts from foreign exchange		99	1 758
Other operating income receipts		198 606	100 678
Personnel expenses		(517 364)	(508 059)
Other general and administrative expenses		(872 768)	(836 371)
(Increase) decrease in operating assets			
Mandatory reserve deposit with the Bank of Russia		(225 605)	(4 454)
Loans to banks		55 256	(950 000)
Loans to customers		(3 678 883)	(2 444 365)
Other assets		25 326	2 694
Increase (decrease) in operating liabilities			
Loans from banks		1 935 833	(1 000 188)
Other borrowings and customers' accounts		(3 728 300)	737 332
Other liabilities		1 844	23 639
Net cash used in operating activities before income tax paid		**(4 157 290)**	**(1 868 810)**
Income tax paid		(254 050)	(234 379)
Cash flows used in operating activities		**(4 411 340)**	**(2 103 189)**
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of property, equipment and intangible assets		(145 650)	(106 726)
Sales of property, equipment and intangible assets		3 381	13 783
Cash flows used in investing activities		**(142 269)**	**(92 943)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Dividends paid		-	(622 272)
Bonds issued		5 000 000	3 000 000
Cash flows provided from financing activities		**5 000 000**	**2 377 728**
Net increase in cash and cash equivalents		**446 391**	**181 596**
Effect of changes in exchange rates on cash and cash equivalents		(1)	(3 866)
Cash and cash equivalents as at the beginning of the year		756 306	578 576
Cash and cash equivalents as at the end of the year	11	**1 202 696**	**756 306**

Koloshenko A.V.
President

Zvereva E.V.
Deputy Chief Accountant

The statement of cash flows is to be read in conjunction with the notes to, and forming part of, the financial statements.

(expressed in thousands of Russian Roubles)

	Share capital	Additional paid-in capital	Retained earnings	Total equity
Balance as at 1 January 2016	5 440 000	1 343 400	2 467 318	9 250 718
Profit and total comprehensive income for the year	-	-	1 117 103	1 117 103
Balance as at 31 December 2016	**5 440 000**	**1 343 400**	**3 584 421**	**10 367 821**
Profit and total comprehensive income for the year	-	-	958 986	958 986
Balance as at 31 December 2017	**5 440 000**	**1 343 400**	**4 543 407**	**11 326 807**

Koloshenko A.V.
President

Zvereva E.V.
Deputy Chief Accountant

1. Background

Organization and operations

AO Toyota Bank (the Bank) was established on 3 April 2007 in the Russian Federation. The Bank has license № 3470 to carry out banking operations in Roubles and foreign currencies and to attract deposits from individuals, Its principal activities are credit operations, customer account maintenance and interbank transactions. The activities of the Bank are regulated by the Bank of Russia. The majority of the Bank's assets and liabilities are located in the Russian Federation.

As at 31 December 2017 the Bank has presence in 70 cities in Russia in 160 dealers' offices that fully covers network of official dealers and certified partners of Toyota and Lexus (2016: 68 cities and 155 dealers' offices).

The Bank is a member of the state deposit insurance system in the Russian Federation and is included in the register of banks-participants of the state deposit insurance system on 28 October 2013 with Registration No.1004.

The average number of people employed by the Bank during 2017 was 145 (2016: 159).

The Bank's registered address is 29, Serebryanicheskaya nab., Moscow, 109028, Russian Federation.

The Bank is part of Toyota Motor Corporation (Japan), one of Japan's largest diversified financial conglomerates. As at 31 December 2017 and 2016, the main shareholder of the Bank is Toyota Kreditbank GmbH (Germany) with 99.94% share.

Related party transactions are detailed in note 26.

Russian business environment

The economic and financial markets of the Russian Federation display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in the Russian Federation. Current economic and politic situation increases local risks for banking operations in the Russian Federation. The Management of the Bank believes that it takes all the necessary efforts to support the economic stability of the Bank in the current environment.

2. Basis of preparation

(a) Statement of compliance

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

(b) Basis of measurement

The financial statements are prepared on the historical cost basis.

(c) Functional and presentation currency

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

The RUB is also the Bank's presentation currency for the purposes of these financial statements.

Financial information presented in RUB is rounded to the nearest thousand.

(d) Use of estimates and judgments

Management makes a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with IFRS. Actual results could differ from those estimates.

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

In particular, information about significant areas of estimation uncertainty and critical judgments in applying accounting policies relates to estimate of impairment allowance for loans to customers as described in note 13 and to estimate of fair values of financial assets and liabilities as described in note 27.

(e) Changes in accounting policies and presentation

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

- *Disclosure Initiative (Amendments to IAS 7).* IAS 7 *Statement of Cash Flows* has been amended as part of the IASB's broader disclosure initiative to improve presentation and disclosure in financial statements. The amendment requires disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes. One way to meet this new disclosure requirement is to provide a reconciliation between the opening and closing balances for liabilities arising from financing activities. However, the objective could also be achieved in other ways.

3. Significant accounting policies

The accounting policies set out below are applied consistently to all periods presented in these financial statements.

(a) Foreign currency transactions

Transactions in foreign currencies are translated to the functional currency at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortized cost in foreign currency translated at the exchange rate at the end of the reporting period. Foreign currency differences arising on retranslation are recognized in profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

(b) Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances (nostro accounts) held with the Bank of Russia and other banks. The mandatory reserve deposit with the Bank of Russia is not considered to be a cash equivalent due to restrictions on its withdrawability. Cash and cash equivalents are carried at amortized cost in the statement of financial position.

(c) Financial instruments

Classification

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

- acquired or incurred principally for the purpose of selling or repurchasing in the near term
- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking
- derivative financial instruments (except for a derivative that is a financial guarantee contract or a designated and effective hedging instruments) or
- upon initial recognition, designated as at fair value through profit or loss.

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

- assets or liabilities are managed, evaluated and reported internally on a fair value basis
- designation eliminates or significantly reduces an accounting mismatch which would otherwise arise or
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

Management determines the appropriate classification of financial instruments in this category at the time of the initial recognition. Derivative instruments and financial instruments designated as at fair value through profit or loss upon initial recognition are not reclassified out of at fair value through profit or loss category. Financial assets that would have met the definition of loan and receivables may be reclassified out of the fair value through profit or loss or available-for-sale category if the Bank has an intention and ability to hold it for the foreseeable future or until maturity. Other financial instruments may be reclassified out of at fair value through profit or loss category only in rare circumstances. Rare circumstances arise from a single event that is unusual.

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

- intends to sell immediately or in the near term
- upon initial recognition designates as at fair value through profit or loss
- upon initial recognition designates as available-for-sale or
- may not recover substantially all of its initial investment, other than because of credit deterioration.

Recognition

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

Measurement

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

Subsequent to initial recognition loans and receivables are measured at amortized cost using the effective interest method.

All financial liabilities are measured at amortised cost. The amortized cost is determined using the effective interest method.

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

Financial assets or liabilities originated at interest rates different from market rates are re-measured at origination to their fair value, being future interest payments and principal repayment(s) discounted at market interest rates for similar instruments. The difference is credited or charged to profit or loss as gains or losses on the origination of financial instruments at rates different from market rates. Subsequently, the carrying amount of such assets or liabilities is adjusted for amortization of the gains/losses on origination and the related income/expense is recorded in interest income/expense within profit or loss using the effective interest method.

Fair value measurement principles

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

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

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

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

Gains and losses on subsequent measurement

For financial assets and liabilities carried at amortized cost, a gain or loss is recognized in profit or loss when the financial asset or liability is derecognized or impaired, and through the amortization process.

Derecognition

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

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

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

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

The Bank writes off assets deemed to be uncollectible.

Offsetting

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

(d) Property and equipment, intangible assets and operating lease

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses.

Depreciation is charged to profit or loss on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. The estimated useful lives are as follows:

Equipment	2-15 years
Fixtures and fittings	3-20 years
Motor vehicles	3-5 years
Leasehold improvement	The lower of economic life or lease term

Acquired intangible assets are stated at cost less accumulated amortization and impairment losses. Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software. Amortization is charged to profit or loss on the straight-line basis over the estimated useful lives of intangible assets and contractual maturity. The estimated useful lives range from 2 to 5 years.

Operating leases under which the Bank does not assume substantially all the risks and rewards of ownership are expensed.

(e) Impairment

Financial assets carried at amortized cost

Financial assets carried at amortized cost consist principally of loans and other receivables (loans and receivables). The Bank reviews loans and receivables to assess impairment on a regular basis. A loan or receivable is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the loan or receivable and that event (or events) has had an impact on the estimated future cash flows of the loan that can be reliably estimated.

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

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

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

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

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

When a loan is uncollectable, it is written off against the related impairment allowance. The Bank writes off a loan balance (and any related impairment allowances) when the loan is overdue more than 721 days and the Management Board made a decision to write it off.

Non financial assets

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

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

(f) Provisions

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

A provision for restructuring is recognized when the Bank has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly.

A contract is recognized as onerous when the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it.

The present obligation under the contract is recognized and measured as a provision. Before a separate provision for an onerous contract is established, the Bank recognizes an impairment loss that has occurred on assets dedicated to that contract.

Future operating costs are not provided for.

(g) Share capital and dividends

Ordinary shares are classified as equity.

Dividends in relation to ordinary shares are reflected as an appropriation of retained earnings in the period when they are declared. The ability of the Bank to declare and pay dividends is subject to the rules and regulations of the Russian legislation.

(h) Taxation

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

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

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for the initial recognition of assets or liabilities that affect neither accounting nor taxable profit. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the temporary differences, unused tax losses and credits can be utilized. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

(i) Income and expense recognition

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

Loan origination fees, loan servicing fees and other fees that are considered to be integral to the overall profitability of a loan, together with the related transaction costs, are deferred and amortized to interest income over the estimated life of the financial instrument using the effective interest method.

Other fees, commissions and other income and expense items are recognized in profit or loss when the corresponding service is provided.

Payments made under operating leases are recognized in profit or loss on a straight-line basis over the term of the lease.

(j) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective as at 31 December 2017, and are not applied in preparing these financial statements. Of these pronouncements, IFRS 9 *Financial instruments* will have the highest impact on the financial statements.

IFRS 9 Financial instruments

General information and impact assessment. IFRS 9 *Financial instruments*, published in July 2014, replaces the existing guidance in IAS 39 *Financial Instruments:* Recognition and Measurement, and includes requirements for classification and measurement of financial instruments, impairment of financial assets and hedge accounting.

The Bank will apply IFRS 9 starting 1 January 2018 and will early adopt the amendments to IFRS 9 on the same date.

The Bank expects that the standard will not have a significant impact on the classification and measurement of financial assets held as at 1 January 2018 and the Bank will continue to measure loans to banks, auto dealers and retail customers using amortized cost in accordance with IFRS 9.

Classification and measurement. IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). The classification of financial assets under IFRS 9 is generally based on the business model in which a financial asset is managed and its contractual cash flow characteristics. The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are not separated. Instead, the whole hybrid instrument is assessed for classification. Equity investments are measured at fair value. IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

Impairment. IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model. The new impairment model applies to financial assets measured at amortised cost and FVOCI, lease receivables, certain loan commitments and financial guarantee contracts. The new impairment model generally requires to recognize expected credit losses in profit or loss for all financial assets, even those that are newly originated or acquired. Under IFRS 9, impairment is measured as either expected credit losses resulting from default events on the financial instrument that are possible within the next 12 months ('12-month ECL') or expected credit losses resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Initial amount of expected credit losses recognized for a financial asset is equal to 12-month ECL (except for certain trade and lease receivables, and contract assets, or purchased or originated credit-impaired financial assets). If the credit risk on the financial instrument has increased significantly since initial recognition, the loss allowance is measured at an amount equal to lifetime ECL.

Financial assets for which 12-month ECL is recognized are considered to be in stage 1; financial assets that have experienced a significant increase in credit risk since initial recognition, but are not defaulted are considered to be in stage 2; and financial assets that are in default or otherwise credit-impaired are considered to be in stage 3.

Measurement of expected credit losses is required to be unbiased and probability-weighted, should reflect the time value of money and incorporate reasonable and supportable information that is available without undue cost or effort about past events, current conditions and forecasts of future economic conditions. Under IFRS 9, credit losses are recognised earlier than under IAS 39, resulting in increased volatility in profit or loss. It will also tend to result in an increased impairment allowance, since all financial assets will be assessed for at least 12-month ECL and the population of financial assets to which lifetime ECL applies is likely to be larger than the population with objective evidence of impairment identified under IAS 39.

Calculation of expected credit losses is likely to be based on the PDxLGDxEAD approach (at least for some portfolios), depending on the type of the exposure, stage at which the exposure is classified under IFRS 9, collective or individual assessment, etc.

Hedge accounting. The general hedge accounting requirements aim to simplify hedge accounting, aligning the hedge accounting more closely with risk management strategies. The standard does not explicitly address macro hedge accounting, which is being considered in a separate project. IFRS 9 includes an accounting policy choice to continue to apply the hedge accounting requirements of IAS 39.

Transition. The classification and measurement and impairment requirements are generally applied retrospectively (with some exemptions) by adjusting the opening retained earnings and reserves at the date of initial application, with no requirement to restate comparative periods.

IFRS 9 is effective for annual reporting periods beginning on or after 1 January 2018. Early adoption of the standard is permitted. The Bank does not intend to adopt the standard earlier.

The Bank has not yet completed the formal assessment of the potential impact of the standard on its financial statements. Currently it is not practicable to estimate the impact that the application of IFRS 9 will have on the Bank's financial statements. The Bank is in the process of development of IFRS 9 implementation plan.

Other standards

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

- IFRS 9 *Financial instruments* covering hedge accounting.
- IFRS 15 *Revenue from Contracts with Customers.*
- IFRS 16 *Leases.*
- *Annual Improvements to IFRSs 2014-2016 Cycle – Amendments to IFRS 1 and IAS 28.*
- *Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2).*
- *Transfers of Investment Property (Amendments to IAS 40).*
- *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28).*
- IFRIC 22 *Foreign Currency Transactions and Advance Consideration*.
- IFRIC 23 *Uncertainty over Income Tax Treatments*.

(expressed in thousands of Russian Roubles)

4. Interest income and expense

	2017	2016
Interest income		
Loans to customers	6 704 464	6 468 102
Loans to banks	132 206	206 331
Total interest income	**6 836 670**	**6 674 433**
Interest expense		
Loans from banks	(1 993 613)	(1 821 626)
Other borrowings and customers' accounts	(1 531 784)	(1 613 495)
Bonds issued	(365 312)	(272 489)
Subordinated borrowings	(118 460)	(118 460)
Total interest expense	**(4 009 169)**	**(3 826 070)**
Net interest income	**2 827 501**	**2 848 363**

Interest income on loans to customers for 2017 includes interest accrued on impaired financial assets totaling RUB 19 654 thousand (2016: RUB 52 472 thousand).

5. Fee and commission income and expense

	2017	2016
Fee and commission income		
Insurance agent services	69 049	370 170
Credit line issuance	32 779	35 595
Other	7 799	4 829
Total fee and commission income	**109 627**	**410 594**
Fee and commission expense		
Promotion of insurance products	(54 771)	(256 674)
Settlement	(61 478)	(67 077)
Other	(1 000)	(8 713)
Total fee and commission expense	**(117 249)**	**(332 464)**
Net fee and commission (expense) income	**(7 622)**	**78 130**

6. Net foreign exchange expense

	2017	2016
Gain on spot transactions	12	1 476
Loss from revaluation of financial assets and liabilities	(150)	(1 654)
Net foreign exchange expense	**(138)**	**(178)**

(expressed in thousands of Russian Roubles)

7. Other operating income

	2017	2016
Recovery of retail loans previously written off	110 410	44 918
Penalties on loans issued	81 558	52 962
Gain on sale of property and equipment and goods for sale	-	10 523
Other income	5 418	3 081
Total other operating income	**197 386**	**111 484**

8. Personnel expenses

	2017	2016
Employee compensation	471 435	434 099
Payroll related taxes	86 100	80 621
Total personnel expenses	**557 535**	**514 720**

9. Other general and administrative expenses

	2017	2016
Services of staffing companies	228 261	201 003
Communications and information services	217 182	173 634
Operating leases	156 452	200 742
Depreciation and amortization (note 14)	99 609	72 399
Collection and servicing of loans	92 911	69 772
Advertising and marketing	66 654	43 640
Consulting and information services	32 338	24 119
Professional services	17 873	18 783
Travel	16 195	10 168
Repairs and maintenance	10 809	14 547
Insurance	7 014	6 649
Office supplies	2 506	3 899
Security	2 876	2 612
Taxes other than income tax	721	1 162
Other	44 855	28 700
Total other general and administrative expenses	**996 256**	**871 829**

(expressed in thousands of Russian Roubles)

10. Income tax expense

	2017	2016
Current year tax expense	267 607	267 047
Deferred taxation movement due to origination and reversal of temporary differences	(1 950)	35 030
Total income tax expense	**265 657**	**302 077**

The applicable tax rate for current and deferred tax in 2017 and 2016 is 20%.

As at 31 December 2017, current tax asset amounts to RUB 25 328 thousand (2016: RUB 51 005 thousand), the Bank has no current tax liabilities (2016: nil).

Reconciliation of effective tax rate

	2017	%	2016	%
Profit before income tax	1 224 643		1 419 180	
Income tax expense at the applicable tax rate	244 929	20.00	283 836	20.00
Non-deductible costs	20 728	1.69	18 241	1.29
Total income tax expense	**265 657**	**21.69**	**302 077**	**21.29**

Deferred tax asset and liability

As at 31 December 2017 and 2016, temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes give rise to net deferred tax liability.

These deductible temporary differences do not expire under current tax legislation.

Movements in temporary differences during 2017 and 2016 are presented as follows.

	1 January 2016	Recognized in profit or loss	31 December 2016	Recognized in profit or loss	31 December 2017
Loans to banks	(108)	108	-	-	-
Loans to customers	(121 846)	(27 101)	(148 947)	(32 934)	(181 881)
Property, equipment and intangible assets	(472)	(467)	(939)	9 439	8 500
Other assets	1 988	(9 124)	(7 136)	(211)	(7 347)
Bonds issued	-	(992)	(992)	(1 034)	(2 026)
Other liabilities	13 491	2 546	16 037	26 690	42 727
Net deferred tax liability	**(106 947)**	**(35 030)**	**(141 977)**	**1 950**	**(140 027)**

(expressed in thousands of Russian Roubles)

11. Cash and cash equivalents

	2017	2016
Nostro accounts with the Bank of Russia	1 111 504	652 456
Nostro accounts with other banks		
- rated AA- to AA+	2 030	1 757
- rated BBB	37 254	52 082
- rated below B+	2 816	12 475
- not rated	49 092	37 536
Total nostro accounts with other banks	**91 192**	**103 850**
Total cash and cash equivalents	**1 202 696**	**756 306**

Ratings in the table above represent the rating scale used by Fitch rating agency. If there is no rating issued by Fitch, the rating assigned by Standard & Poor's or Moody's is taken and transformed into the rating scale used by Fitch.

None of cash and cash equivalents are impaired or past due.

As at 31 December 2017, there is one bank, whose balances individually exceed 10% of total cash and cash equivalents. The gross value of these balances is RUB 1 111 504 thousand or 92% of total cash and cash equivalents (2016: RUB 652 456 thousand or 86%).

Mandatory reserve deposit with the Bank of Russia

The mandatory reserve deposit is a non-interest bearing deposit issued in accordance with the regulations of the Bank of Russia and which withdrawability is restricted. As at 31 December 2017, mandatory reserve deposit with the Bank of Russia is RUB 238 903 thousand (2016: RUB 13 303 thousand).

12. Loans to banks

As at 31 December 2017 and 2016 loans to banks are RUB 3 343 251 thousand and RUB 3 400 836 thousand and are placed with the Bank of Russia. These loans are not impaired or overdue.

13. Loans to customers

	2017	2016
Loans to auto dealers	7 770 868	10 829 039
Retail loans		
Auto loans	44 818 654	38 373 303
Total retail loans	**44 818 654**	**38 373 303**
Gross loans to customers	**52 589 522**	**49 202 342**
Impairment allowance	(1 011 057)	(1 256 730)
Total net loans to customers	**51 578 465**	**47 945 612**

Movements in the impairment allowance for loans during 2017 and 2016 are as follows:

	Loans to auto dealers	Retail loans	Total
Balance as at 1 January 2016	597 999	819 324	1 417 323
Net (recovery) charge for the year	(205 367)	443 998	238 631
Write-offs	–	(399 224)	(399 224)
Balance as at 31 December 2016	**392 632**	**864 098**	**1 256 730**
Net (recovery) charge for the year	(63 378)	301 707	238 329
Write-offs	–	(484 002)	(484 002)
Balance as at 31 December 2017	**329 254**	**681 803**	**1 011 057**

(expressed in thousands of Russian Roubles)

Credit quality of loans to customers

The table below provides information on the credit quality of loans to customers as at 31 December 2017:

	Gross loans	Impairment allowance	Net loans	Impairment allowance to gross loans, %
Loans to auto dealers				
Not overdue loans without individual signs of impairment	7 654 621	(264 956)	7 389 665	3.46
Impaired loans, overdue more than 180 days	116 247	(64 298)	51 949	55.31
Total loans to auto dealers	**7 770 868**	**(329 254)**	**7 441 614**	**4.24**
Retail loans				
Auto loans				
- not overdue	43 449 072	(257 773)	43 191 299	0.59
- overdue less than 30 days	721 871	(18 347)	703 524	2.54
- overdue 30-59 days	114 005	(16 022)	97 983	14.05
- overdue 60-89 days	48 899	(11 914)	36 985	24.36
- overdue 90-179 days	92 265	(48 184)	44 081	52.22
- overdue more than 180 days	392 542	(329 563)	62 979	83.96
Total retail loans	**44 818 654**	**(681 803)**	**44 136 851**	**1.52**
Total loans to customers	**52 589 522**	**(1 011 057)**	**51 578 465**	**1.92**

The table below provides information on the credit quality of loans to customers as at 31 December 2016:

	Gross loans	Impairment allowance	Net loans	Impairment allowance to gross loans, %
Loans to auto dealers				
Not overdue loans without individual signs of impairment	10 721 329	(284 922)	10 436 407	2.66
Impaired loans, overdue more than 180 days	107 710	(107 710)	-	100.00
Total loans to auto dealers	**10 829 039**	**(392 632)**	**10 436 407**	**3.63**
Retail loans				
Auto loans				
- not overdue	36 798 926	(221 540)	36 577 386	0.60
- overdue less than 30 days	689 228	(20 909)	668 319	3.03
- overdue 30-59 days	103 366	(15 666)	87 700	15.16
- overdue 60-89 days	54 360	(13 985)	40 375	25.73
- overdue 90-179 days	90 541	(47 929)	42 612	52.94
- overdue more than 180 days	636 882	(544 069)	92 813	85.43
Total retail loans	**38 373 303**	**(864 098)**	**37 509 205**	**2.25**
Total loans to customers	**49 202 342**	**(1 256 730)**	**47 945 612**	**2.55**

Key assumptions and judgments for estimating the loan impairment

Loans to auto dealers

Loan impairment results from one or more events that occurred after the initial recognition of the loan and that have an impact on the estimated future cash flows associated with the loan, and that can be reliably estimated. Loans without individual signs of impairment do not have objective evidence of impairment that can be directly attributed to them.

The objective indicators of loan impairment for loans to auto dealers include the following:

- a breach of contract, such as a default or delinquency in interest or principal payments
- significant deterioration of the financial position of the borrower
- deterioration in business environment, negative changes in the borrower's markets
- it becomes probable that the borrower will enter bankruptcy or other financial reorganization.

(expressed in thousands of Russian Roubles)

The Bank estimates the loan impairment for loans to auto dealers based on the analysis of the future cash flows for impaired loans and based on its past loss experience for portfolios of loans for which no indications of impairment has been identified adjusted on current economic environment and financial position of the borrowers.

Changes in these estimates could affect the loan impairment allowance. For example, to the extent that the net present value of the estimated cash flows differs by plus/minus one percent, the impairment allowance on loans to auto dealers as at 31 December 2017 would be RUB 74 416 thousand lower/higher (2016: RUB 104 364 thousand lower/higher).

Retail loans

The Bank estimates the impairment allowance for retail loans based on its past historical loss experience on each type of loan. The significant assumptions used by management in determining the impairment allowance for retail loans include that loss migration rates are constant and can be estimated based on the historic loss probability of default for the past 9 months and recovery rates on default loans are estimated based on all available historic data.

Changes in these estimates could affect the loan impairment allowance. For example, to the extent that the net present value of the estimated cash flows differs by minus one percent, the impairment allowance on retail loans as at 31 December 2017 would be RUB 441 369 thousand higher (2016: RUB 375 092 thousand higher).

Analysis of collateral

Loans to auto dealers

The following table provides the analysis of loans to auto dealers, net of impairment, by types of collateral as at 31 December 2017 and 2016:

	2017	% of loans to auto dealers	2016	% of loans to auto dealers
Motor vehicles	6 733 493	90.48	9 482 325	90.86
Real estate	708 121	9.52	954 082	9.14
	7 441 614	**100.00**	**10 436 407**	**100.00**

The amounts shown in the table above represent the carrying value of the loans, and do not necessarily represent the fair value of the collateral.

For loans to auto dealers without individual signs of impairment the fair value of collateral was estimated at the inception of the loans and was not adjusted for subsequent changes to the reporting date. The recoverability of these loans is primarily dependent on the creditworthiness of the borrowers rather than the value of collateral, and The current value of the collateral does not impact the impairment assessment.

As at 31 December 2017 and 2016, the Bank identified signs of impairment for loans issued to one auto dealer.

Retail loans

Auto loans are secured by the underlying cars.

The Bank assesses the fair value of collateral as at loan origination date. The management believes that the fair value of collateral is at least equal to the carrying amount of individual loans as at the reporting date.

In 2017 the Bank took possession of collateral for loans to individuals with a net carrying amount of RUB 9 922 thousand (2016: RUB 1 552 thousand). As at 31 December 2017, the carrying amount of repossessed collateral amounts to RUB 5 821 thousand (2016: RUB 1 522 thousand).

Significant credit exposures

Loans to customers are issued primarily to individuals and auto dealers operating in the Russian Federation.

As at 31 December 2017 and 2016 the Bank has no borrowers or groups of related borrowers whose loan balances individually exceed 10% of total loans to customers.

Loans maturities

The maturity of loans to customers is presented in note 21.

(expressed in thousands of Russian Roubles)

14. Property, equipment and intangible assets

The following table provides information on property, equipment and intangible assets as at 31 December 2017 and 2016:

	Equipment	Fixtures and fittings	Motor vehicles	Software licenses	Leasehold improve ments	Total
Cost						
Balance as at 1 January 2016	153 135	105 881	38 749	280 887	25 939	604 591
Additions	22 853	681	9 005	74 958	–	107 497
Disposals	(1 480)	(76)	(15 758)	(135 582)	–	(152 896)
Balance as at 31 December 2016	**174 508**	**106 486**	**31 996**	**220 263**	**25 939**	**559 192**
Additions	2 789	296	3 609	138 956	–	145 650
Disposals	(4 060)	(299)	(4 642)	(1 894)	–	(10 895)
Balance as at 31 December 2017	**173 237**	**106 483**	**30 963**	**357 325**	**25 939**	**693 947**
Depreciation						
Balance as at 1 January 2016	**132 846**	**60 896**	**23 523**	**175 243**	**20 474**	**412 982**
Depreciation and amortization charge	8 890	17 482	2 459	38 103	5 465	72 399
Disposals	(1 480)	(76)	(12 499)	(135 582)	–	(149 637)
Balance as at 31 December 2016	**140 256**	**78 302**	**13 483**	**77 764**	**25 939**	**335 744**
Depreciation and amortization charge	11 349	17 042	3 227	67 991	–	99 609
Disposals	(4 060)	(299)	–	(1 848)	–	(6 207)
Balance as at 31 December 2017	**147 545**	**95 045**	**16 710**	**143 907**	**25 939**	**429 146**
Carrying value as at:						
31 December 2016	34 252	28 184	18 513	142 499	-	223 448
31 December 2017	25 692	11 438	14 253	213 418	-	264 801

15. Other assets

	2017	2016
Financial assets		
Settlements with suppliers	57 531	99 199
Subventions receivable	37 646	-
Guarantee deposit	21 221	27 088
Advances	2 954	17 800
Others	31 213	32 034
Total other assets	**150 565**	**176 121**

As at 31 December 2017 and 2016, the Bank doesn’t have overdue and/or impaired other assets.

16. Loans from banks

As at 31 December 2017, loans from banks amount to RUB 19 957 380 thousand. Loans totaling RUB 15 777 771 thousand or 79% of total loans from banks are received from four banks, that individually contribute above 10% to total loans from banks.

As at 31 December 2016, loans from banks amount to RUB 18 017 703 thousand. Loans totaling RUB 11 150 619 thousand or 62% of total loans from banks are received from four banks, that individually contribute above 10% to total loans from banks.

(expressed in thousands of Russian Roubles)

17. Other borrowings and customers' accounts

	2017	2016
Borrowings from Toyota Motor Finance (Netherlands) B. V.	14 052 492	17 843 667
Settlement accounts of auto dealers	595 667	1 015 018
Current accounts of individuals	871 873	410 461
	15 520 032	**19 269 146**

18. Bonds issued, subordinated borrowings and reconciliation of changes in liabilities and cash flows from financing activities

On 30 November 2017 the Bank issued coupon documentary bearer bonds totaling RUB 5 000 000 thousand and maturing on 2 December 2020. An annual coupon rate for 1-6 coupon payments is 8.05%. The Fitch Ratings rated the issue as "A-".

On 10 March 2016 the Bank issued coupon documentary bearer bonds totaling RUB 3 000 000 thousand and maturing on 13 March 2019 with an early redemption option on 12 March 2018. An annual coupon rate for 1-4 coupon payments is 10.75% (annual coupon rate for 5 and 6 coupon payments is determined by the Bank). The Fitch Ratings rated the issue as "A-". On 12 March 2018 the Bank redeemed coupon documentary bearer bonds totaling RUB 3 000 000 thousand.

Subordinated borrowings are provided by Toyota Motor Finance (Netherlands) B.V., mature in 2018 and 2019 and carry an annual interest rate of 8.46%. In case of bankruptcy, the repayment of the subordinated borrowings will be made after repayment in full of all other liabilities of the Bank. In 2017 and 2016 the Bank had no new subordinated borrowings and made no repayments of principle.

The reconciliation of changes in liabilities and cash flows from financing activities is presented in the table below:

	Bonds issued	Subordinated borrowings	Total
Balance as at 1 January 2017	3 094 886	1 414 393	4 509 279
Changes from cash flows from financing activities			
Bonds issued	5 000 000	-	5 000 000
Total changes from cash flows from financing activities	**5 000 000**	**-**	**5 000 000**
Borrowing costs	(10 120)	-	(10 120)
Interest expense	365 312	118 460	483 772
Interest paid	(327 050)	(118 298)	(445 348)
Balance as at 31 December 2017	**8 123 028**	**1 414 555**	**9 537 583**

19. Other liabilities

	2017	2016
Financial liabilities		
Settlements with suppliers	250 562	226 647
Non-financial liabilities		
Liability on bonus to employees	51 709	11 539
Provision for unused vacations	19 914	22 155
Liability under buy-back program	-	364
Total non-financial liabilities	**71 623**	**34 058**
Total other liabilities	**322 185**	**260 705**

Several Bank's products provide vehicle buy back option. As at 31 December 2017, the carrying amount of these loans to customers totals RUB 42 181 thousand (2016: RUB 496 369 thousand). On these products the dealer guarantees customer to buy back a vehicle financed through the loan issued by the Bank for a residual payment up to 60% of initial car price. The Bank is obliged to compensate a dealer a difference between the market price and a pre-agreed residual amount if the market price is lower. As at 31 December 2017, the Bank estimated its future liability under these loans to be nil (2016: RUB 364 thousand).

20. Share capital

As at 31 December 2017 and 2016, the authorized, issued and outstanding share capital comprises 1 600 000 ordinary shares. All shares have a nominal value of RUB 3 400, rank equally and carry one vote per share at annual and extraordinary general meetings of the Bank's shareholders.

In 2017 and 2016 the Bank did not declare any dividends.

21. Risk management, corporate governance and internal control

Corporate governance framework

The Bank is established as a joint stock company in accordance with legislation of the Russian Federation and is a non-public joint stock company. The supreme governing body of the Bank is the General meeting of shareholders. Annual General meetings of shareholders are held annually. Extraordinary General meetings of shareholders are called on request of the Supervisory Board, internal or external auditors, and shareholders owning at least 10% of voting shares of the Bank. The General meeting of shareholders makes strategic decisions on the Bank's operations.

Russian legislation and Bank's Charter list decisions that are exclusively approved by the General meeting of shareholders and that are approved by the Supervisory Board.

General meeting of shareholders. The General meeting of shareholders exclusively approves the following matters:

- introduction of amendments and addenda to the Charter or approval of the new edition of the Charter
- composition of the Supervisory Board, electing its members and their early resignation
- determination of quantity, par value and type of shares and rights assigned to these shares
- decisions on change of charter capital
- assignment of members of the Management Board and President and their early resignation
- electing of controller and his early resignation
- approval of external auditor
- decisions on distribution of profits and dividends payments
- approval of annual reports and annual financial statements
- approval of significant self-dealing transactions
- decision on participation in associations and other unions of commercial enterprises
- approval of certain internal policies of the Bank, which regulate the Bank's operations
- other matters set by Federal Law № 208-FZ *On Joint Stock Companies* dated 26 December 1995.

The above matters are within the sole responsibility of the General meetings of shareholders and shall not be delegated to the executive body or Supervisory Board or executive bodies of the Bank, except for the issues specified in Federal Law № 208-FZ *On Joint Stock Companies* dated 26 December 1995.

Supervisory Board. As at 31 December 2017, the Supervisory Board of the Bank comprise:

- Hironobu Obata – Chairman of the Supervisory Board
- Christian Ties Ruben – member of the Supervisory Board
- Vatanabe Khitoshi – member of the Supervisory Board
- Hidenori Ozaki – member of the Supervisory Board
- Ivo Josko Ljubica – member of the Supervisory Board

In 2017 there composition of the Supervisory Board did not change.

The Supervisory Board exclusively approved the following matters:

- setting priority directions of the Bank's activities
- convening annual and extraordinary General meetings of shareholders, except as required by law
- approval of agenda for General meetings of shareholders and decisions on other organizational matters related to General meetings of shareholders, as required by law and Bank's Charter
- decisions on issue of bonds and other securities by the Bank
- recommendations on dividends amount and payment procedures
- utilization of the reserve and other funds
- approval of internal documents, except when required to be approved by the General meeting of shareholders or when the Charter requires the approval by the executive bodies

- opening and closing of branches and representative offices
- approving significant self-dealing transactions, except for transactions, that are required to be approved by the General meetings of shareholders
- approval of Bank's risk and capital management strategy and risk management procedures for those risks that are most significant to the Bank and control of implementation of these procedures
- approval of application of banking risk management techniques and models for quantitative assessment of risks, including assets and liabilities and unrecognized assets and commitments, and of scenarios and results of stress testing
- approval of conflict of interest preventing procedure
- approval of financial recovery and business continuity plans
- approval of the Head of the Internal Audit Service and internal audit working plan
- approval of staff policy including remuneration of management
- other matters, as required by legislation and Bank's Charter.

Executive bodies of the Bank. General activities of the Bank are managed by the sole executive body (the President) and collective executive body (the Management Board of the Bank).

The executive bodies of the Bank are responsible for implementation of decisions of the General meeting of the shareholders and the Supervisory Board. Executive bodies of the Bank report to the Supervisory Board and to the General meeting of shareholders. The authorities of executive bodies are set by the legislation and Bank's Charter.

The President of the Bank acts on behalf of the Bank without power of attorney, represents interests of the Bank, concludes deals, approves staff, issues orders, and gives instructions binding for all employees of the Bank.

As at 31 December 2017 and 2016, the Management Board includes:

- Alexander Koloshenko – the Chairman of the Management Board
- Yulia Sorokina – Management Board member
- Anna Shengelevich – Management Board member.

In 2017 and 2016, there were no changes in composition of the Management Board.

Internal control policies and procedures

The internal controls are in place to ensure:

- appropriate and comprehensive risk assessment and management
- appropriate business and accounting and financial reporting functions, including appropriate authorization, processing and recording of transactions
- completeness, accuracy and timeliness of accounting records, managerial information, regulatory reports, etc.
- reliability of IT-systems, data and systems integrity and protection
- prevention of fraudulent or illegal activities, including misappropriation of assets
- compliance with laws and regulations.

The internal control comprises:

- the General meeting of shareholders
- the Supervisory Board
- Executive bodies: the President and the Management Board
- the Controller
- the Chief Accountant and the Deputy Chief Accountant
- Other employees, functions and services performing internal control in accordance with the responsibilities set by internal policies and procedures, including:
  - the Internal Audit Service
  - the officer, responsible for anti-money laundering procedures and financing of terrorism prevention and the subordinate Financial monitoring function
  - the Compliance officer
  - the Credit policy and risk management department, and
  - other divisions and (or) employees responsible for internal control.

The Supervisory and Management Boards have responsibility for the development, implementation and maintaining of internal controls in the Bank that are appropriate for the scale, nature and complexity of operations.

Management is responsible for identifying and assessing risks, designing controls and monitoring their effectiveness. Management monitors the effectiveness of the Bank's internal controls and periodically implements additional controls or modifies existing controls as considered necessary.

The Internal Audit Service performs continuous and independent assessment of the operating effectiveness of internal control, identifies failures and deficiencies in the control environment and monitors their timely resolution and correction. The Internal Audit Service functions include:

- audit and assessment of efficiency of the internal control as a whole, fulfillment of the decisions of the Bank's management bodies
- audit of efficiency of assessment of banking risks methodology and risk management procedures, regulated by internal documents (methods, programs, rules and procedures for banking operations and transactions, and for the management of banking risks)
- audit of reliability of internal control system over automated information systems
- audit and testing of fairness, completeness and timeliness of accounting and reporting functions and the reliability (including the accuracy, completeness and timeliness) of the collection and submission of financial information and reporting
- audit of existing procedures aimed at securing Bank's property
- assessment of economic feasibility and efficiency of operations and other deals
- audit of internal control processes and procedures
- audit of internal control and risk management functions.

The Internal Audit Service is independent from management and reports directly to the Supervisory Board. The results of Internal audit reviews are discussed with relevant business process managers, with summaries submitted to the Supervisory Board, the President and the Management Board. The frequency and consistency of reports prepared by the Internal Audit Service during 2017 was in compliance with the Bank's internal documentation. The Supervisory Board and executive management periodically discussed reports prepared by the Internal Audit Service, and considered proposed corrective actions. The reports included observations made by the Internal Audit Service as to their assessment of the effectiveness of the Bank's procedures and methodologies, and recommendations for improvement.

The internal control function is performed by the Compliance officer. The Compliance officer is subordinated to and reports to the President. The Compliance officer is primarily focused on regulatory risks faced by the Bank. The Compliance officer performs the following:

- identification of compliance and regulatory risks
- monitoring of events associated with regulatory risk, including probability of occurrence and quantitative assessment of their consequences
- monitoring of regulatory risk
- recommendations on regulatory risk management
- coordination of and participation in development of activities aimed at mitigation of regulatory risk
- monitoring of efficiency of regulatory risk management
- participation in preparation of internal documents on regulatory risk management, anti-corruption, compliance with corporate behavior rules, code of professional ethics and minimization of conflicts of interest
- analysis of dynamics of clients' complaints
- analysis of economic feasibility of agreements with suppliers
- participation in communications with authorities, self-regulated organizations, associations and financial market participants.

Russian legislation, including Federal Law dated 2 December 1990 No 395-1 *On banks and banking activity* and Direction of the Bank of Russia dated 1 April 2014 No 3223-U *On Requirement to Head of Risk Management Service, Head of Internal Control Service, Head of Internal Audit Service of the Credit Organization* establish the professional qualifications, business reputation and other requirements for the members of the Supervisory and Management Boards, Heads of the Internal audit, Internal control function, risk management function and other key management personnel. As at the date of these financial statements, the heads of the respective functions comply with the requirements, set by the law and regulations of the Bank of Russia in respect of business reputation.

The Bank developed policies and procedures to ensure appropriate operations and compliance with relevant legal and regulatory requirements, including the following areas:

- requirements for appropriate segregation of duties, including independent authorization of transactions
- requirements for the recording, reconciliation and monitoring of transactions
- compliance with regulatory and other legal requirements
- documenting of controls and procedures
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address identified risks
- requirements for the reporting of operational losses and proposed remedial action
- development of contingency plans
- training and professional development
- ethical and business standards and
- risk mitigation, including insurance where this is effective.

The Bank maintains a hierarchy of requirements for authorization of transactions depending on their size and complexity. A significant portion of operations is automated and a system of automated controls is implemented.

Management believes that the Bank complies with the requirements of the Bank of Russia in respect of internal control systems, including requirements related to the Internal Audit Service and internal control system is appropriate for the scale, nature and complexity of operations.

Information about the risks accepted by the Bank, methods of their identification, measurement, risk and capital management

The Bank has established a risk and capital management system through the implementation of internal procedures for assessment of capital adequacy (“IPACA”). Requirements over these procedures are set in the Instruction of the Bank of Russia No. 3624-U dated 15 April 2015. IPACA are correspondent to the size of operations performed by the Bank, level and combination of risks.

The objectives of risk and capital management system are as follows:

- identify, evaluate and aggregate the most significant risks that may result in losses material for the assessment of capital adequacy and to control their exposures
- evaluate the adequacy of Bank’s available capital to cover significant risks and new types (additional volumes) of risks, the adoption of which is due to the implementation of the activities under the Bank’s development strategy
- plan equity amount based on the results of a comprehensive assessment of significant risks, Bank’s testing in relation to internal and external risk factors, the Bank’s development strategy and legislative requirements.

IPACA are integrated in the Bank’s strategic planning system, i.e. results of completion of IPACA are an integral part of the Bank’s governance and decision-making processes (development of the Bank’s strategy) as a basis for measurement of capital required to cover significant and potential risks. In the process of development of the Bank’s strategy the expected IPACA results are subject to a review in order to ensure that the coverage of risks remains adapted to the new conditions, changing nature and scale of transactions, diversity and complexity of Bank’s activities.

The Supervisory Board approves the Bank’s risk and capital management strategy, including as it relates to maintenance of sufficient own funds (capital) and liquidity to cover risks across the Bank and related to specific business activities, as well as approves the risk management policies of the Bank and controls over their implementation.

Management Board is responsible for the implementation of the risk management strategy and policy of the Bank, approved by the Bank's Supervisory Board, identifies, monitors and control risks to which the Bank is exposed, regularly reports to the Supervisory Board on Bank's risk exposure, as well as ensures compliance with IPACA and maintenance of the capital adequacy at the level established by the internal documents of the Bank. Management Board approves duties and composition of collective risk management bodies.

The risk and capital management system provides a functional segregation between the collective risk management bodies.

The Risk Management Committee responsibilities include:

- assessment (definition of acceptable level) and control of the levels of the risks taken by the Bank
- recommendations to the Supervisory Board on risk management
- review of risks reports provided by the Bank's business units
- approval and development of specific actions (including instructions to the Bank's business units) to minimize risks throughout Bank's activities
- review and approval of draft documents regulating risk management and amendments to them
- control over execution of decisions made at the Committee meetings.

The Credit Committee responsibilities include:

- control over credit risks arising in the course of Bank's activities
- approval or amendment (if required) of conditions, forms, facilities, terms, volume of lending depending on the level of credit risk
- decisions on change of collateral under the in-force loan and pledge agreements
- implementation of requirements for means of security loans' collection and other obligations
- development and approval of decisions on quality of Bank's loan portfolio and its effective use
- development of Bank's short- and mid-term lending strategy in accordance with business development program
- review and approval of draft internal documents regulating Bank's lending activities and of amendments to these drafts
- control over execution of decisions made at Credit Committee meetings
- review and approval of new projects and programs, changes of projects and programs, relate to development of lending activities of the Bank
- review and approval of reports on breaches, identified in the credit process, and issues related to quality and completeness of collecting and keeping credit documentation and borrower loan files.

The Asset and Liability Committee responsibilities include:

- Bank's liquidity control and effective management
- analysis of effectiveness of Bank's business units involved in the liquidity management based on the management reporting
- control over complying with target rates and status of actual ratios
- control and cost-benefit analysis of assets and liabilities transactions performed by the Bank
- analysis of Bank's assets and liabilities structure
- strategy compliance control of management of currency, interest rate, liquidity, off-balance sheet and other financial risks (except for credit risks).

The Bank ensures segregation of risk acceptance and management functions between business units, in such a way that performing of risk bearing transactions (deals) and risk management are not functions of one business unit.

Credit Policy and Risk Management Department performs general risk management and controls the application of common principles and methods for identification, assessment, management and reporting on the risks. This department develops the risk assessment methodology, carries out independent risk analysis of products, programs and limits on specific clients/operations, performs the portfolio risk analysis, as well as performs risks control function: sets limits, controls their compliance, prepares reports on significant risks levels, which are regularly reported to the Supervisory Board, the Management Board and the Risk Management Committee.

Credit Policy and Risk Management Department is the Bank's business unit, which operates on a regular basis. Head of the Department is subordinated to and reports to the President of the Bank and complies with the Bank of Russia's qualification requirements and requirements on business reputation.

The President of the Bank determines the structure and staffing plan of the Credit Policy and Risk Management Department. The Corporate Risk Management Department, the Retail Risk Management Department and Information Security Service are subordinated to the Head of the Department.

As at 1 January 2018, the Bank's Internal Audit Service was subordinated to, and reported to, the Supervisory Board, and the risk management functions were not subordinated to, and did not report to, divisions accepting relevant risks in accordance with regulations and recommendations issued by the Bank of Russia.

The Bank's internal documentation, effective on 1 January 2018, establishing the procedures and methodologies for identifying and managing the Bank's significant risks, and for stress-testing was approved by the authorized management bodies of the Bank in accordance with regulations and recommendations issued by the Bank of Russia.

In 2017 the annual risk analysis was performed and the following significant risks were determined:

- **Credit risk** is the risk arising from the possibility of a borrower's or counterparty's failure to discharge its obligations to the Bank.
- **Market risk** is the risk of financial losses due to the change in current (fair) value of financial instruments, as well as in foreign exchange rates and/or precious metals' accounting prices.
- **Operational risk** is the risk of losses resulting from failures and deficiencies in Bank's internal operational procedures, malfunction of information and other systems or from impact of external events on operations of the Bank.
- **Liquidity risk** is the risk that the Bank will be unable to finance its activities, i.e. to ensure the growth of assets and to meet its obligations as they fall due without incurring losses in the amount threatening the Bank's financial stability.
- **Concentration risk** is defined as the risk arising out of the Bank's large risk exposures, which, if realized, may lead to significant losses that could threaten Bank's financial solvency and its ability to continue as a going concern.
- **Interest risk** (interest rate risk) is the risk of deterioration of Bank's financial position through the decrease of equity amount, income level, assets value as a result of changes in market interest rates.
- **Business risk** is the risk of losses due to unfavorable changes in the general economic environment (for example, changes in consumers' behavior, intensity of competition, technological progress, etc.) and (or) due to general macroeconomic conditions.

In determining the significant risks the Bank also identified some other non-financial risks which are not significant for the Bank:

- **Risk of loss of business reputation (reputational risk)** – decrease in number of clients (counterparties) as a result of negative perception of the Bank's creditworthiness, quality of services provided or business as whole.
- **Compliance risk (regulatory risk)** – risk of financial losses of the Bank arising out of non-compliance with the legislation, Bank's internal documents, standards of self-regulatory organizations and also from application of sanctions and (or) other corrective actions from supervisory authorities.
- **Cross-border risk** – risk of freezing of accounts by the foreign state or the Russian legislation or intervention in the transfer of cash funds abroad.
- **Payment processing risk** arises in case of violation and termination of contracts with banks-counterparties and/or payment systems related to acceptance of payment as part of retail loan repayment.
- **Residual value risk** – risk of additional expenses required to compensate the difference between car's repurchase and actual prices at the date of buy-back (residual value) assuming that repurchase price exceeds the residual value.
- **Strategic risk** – risk of adverse changes in Bank's operational results due to wrong decisions made by the management of the Bank, including as part of development, approval and implementation of the Bank's development strategy, improper execution of the decisions made and also inability of the Bank's management to react to changes in external factors.

The general principles for the implementation of the IPACA are defined in the Bank's internal document "Risk and Capital Management Strategy" ("the Strategy").

The strategy aims at risks identification, analysis and management, at setting of risks limits and related controls, as well as at regular assessment of risk levels and their compliance with established limits. Risk management policies and procedures are reviewed on a regular basis to reflect the changes in the market environment, offered banking products and services, and emerging best practices. As a part of annual update of risk management procedures, the Supervisory Board approved new values of planning capital adequacy ratio, target significant risk levels, as well as alarming values and capital limits to cover risks by areas of activity, types of significant risks and business units.

Internal procedures for assessment of the Bank's capital adequacy include:

- procedures for capital management, including the definition of the planned (target) level of capital, current capital requirements, the assessment of capital adequacy by the types of significant risks and activities of the Bank
- system for monitoring significant risks, capital adequacy and compliance with risk limits
- Bank's financial reports prepared within implementation of IPACA.

The Bank determines risk appetite in order to ensure stable going concern basis in the longer term. Risk appetite is determined by the risk and capital management strategy of the Bank based on total ultimate risk accepted by the Bank and targets established in the Bank's business development strategy.

Risk appetite for determination of requirements for specified significant risks and aggregated required capital is determined in terms of qualitative and quantitative indicators.

Based on risk appetite indicators the Bank determined planning (target) capital level, planning capital structure, sources of funding, planning (target) capital adequacy ratio, as well as planning (target) risk levels and target risk structure. As a part of determining planning (target) capital level, planning capital structure, planning (target) capital adequacy ratio the Bank relies on the business cycle phase, assessment of current capital requirements, required for covering significant risks (the "amount of required capital"), as well as considers possible requirements for attracting additional capital and available sources of funding to cover significant risks taking into account business development guidelines, planning (target) risk levels and target Bank's risk structure established in the business development strategy.

To assess capital adequacy, the Bank develops procedures for reconciliation of total required capital and amount of available capital. The available capital, with consideration to capital's risk appetite indicator, shall cover total amount of required capital. The total amount of capital required for the Bank is determined based on aggregated assessment of capital requirements in relation to significant risks.

For monitoring of own funds (capital) adequacy the Bank has developed a "Capital allocation procedure", that sets out capital allocation procedures through the use of system of limits throughout business activities, types of significant risks, and functions, whose activities require risks taking.

As part of capital allocation process, the Bank ensures that reserve capital is available to cover those risks, that are not assessed through quantitative methods, as well as the risks that cannot or are difficult to be allocated to the business units of the Bank (for example, operational risk), as well as to facilitate implementation of business development activities.

The Bank controls compliance with risk limits by its business units. As a part of control over limits established, the Bank develops system of indicators revealing high degree of using the limit by business units (alarm values).

A list of corrective measures is designed for each alarm value and depends on how close the use of a limit is to the alarm value, for example:

- take actions to decrease the level of risk taken or by types of activities and relevant business unit
- reallocation of capital between types of significant risks and/or types of activities and relevant business units
- increase of amount of available capital of the Bank.

Results on limits control (instances of reaching alarm values, exceeding limits) are included in the Bank's reports on IPACA and are reported to the Supervisory Board, Bank's executive bodies, heads of Bank's business units engaged in risks taking and risks management.

As at 31 December 2017 the Bank has a reporting system, prepared under IPACA and which also includes reports on: results of IPACA, results of stress-testing, significant risks, amount of capital, results of capital adequacy assessment and complying with statutory ratios.

The frequency and consistency of reports prepared by risk management functions and the Internal Audit Service during 2017 within the IPACA was in compliance with the Bank's internal documentation. The reports included observations made by the Bank's risk management functions and Internal Audit Service as to their assessment of the effectiveness of the Bank's procedures and methodologies, and recommendations for improvement.

As at 31 December 2017, the Supervisory Board and executive management of the Bank had responsibility for monitoring the Bank's compliance with risk limits and capital adequacy ratios as established by the Bank's internal documentation. With the objective of monitoring effectiveness of the Bank's risk management procedures and their consistent application during 2017 the Supervisory Board and executive management of the Bank periodically discussed reports prepared by the risk management functions and Internal Audit Service, and considered proposed corrective actions.

Credit risk

Credit risk is the risk arising from the possibility of a borrower's or counterparty's failure to discharge its obligations to the Bank.

The Bank has developed a credit policy and procedures regulating assessment of the borrower's financial position, loan decision-making procedures, and procedures for controlling timely repayment of loans.

Credit risks management system is based on the following principles:

- the risk is accepted in accordance with the approved Risk and Capital Management Strategy
- the principle of qualitative and quantitative assessment of risks
- the principle of constant monitoring of the accepted credit risks and control over the procedures used, as well as the loan portfolio concentration management
- use of unified loan agreement templates approved by the Legal Department and Credit Policy and Risk Management Department
- the principle of limiting the amount of unforeseen losses covered by capital with a given probability for a certain period.

Basic actions for credit risk management:

- preliminary assessment of the borrower's creditworthiness and his future ability to service a loan (using scoring and (or) rating models), as well as quantitative and qualitative assessment of the collateral provided
- loan portfolio monitoring
- definition of credit limits
- differentiation of employees' authority.

Credit risk management tools are divided into risk assessment tools and risk management tools (strategic and operational).

In order to assess the risk and calculate the amount of regulatory capital to cover the default risk, the Bank uses a standardized credit risk assessment approach established by the Regulation of the Bank of Russia No. 180-I, as well as the Provisions of the Bank of Russia No. 590-P and 283-P. This method is used for all the Bank's activities, including corporate, retail and interbank lending.

The main tool of a credit risk strategic management is an allocation of a portion of the available capital to cover it. In the process of planning the allocation of capital to the areas of activity, the Bank's Management Board approves the restrictions on the use of available capital to cover the credit risk.

Limits on the capital allocated for covering credit risk are supplemented with operational instruments (measures) that ensure that the risk is taken strictly within the limits set by the Bank, that is, with proper monitoring and control.

The Bank has established a system of limits, particularly credit risk limits and concentration risk limits, since they are of a common nature.

The general limits include regulatory credit limits based on the mandatory ratios N1, N6, N7, N9.1, N10.1, as well as the limits on major concentration of risk by geographic location of borrowers (individuals and legal entities).

In corporate lending, the Bank establishes credit limits per borrower or a group of related borrowers, a group of borrowers and by industry in which borrower operates.

In retail lending, the Bank establishes a limit on the maximum amount of outstanding loan for loans to one individual borrower, as well as limits on the share of total outstanding loans for the retail loan portfolio of the following types of loans:

- for the purchase of a car under the credit products that do not require mandatory insurance of the collateral for CASCO (products "Less CASCO")
- for purchase of used cars
- for credit products with a residual payment or 2 payment periods.

In interbank lending, the Bank establishes credit limits for counterparty banks, including the maximum limit for one counterparty bank.

As of 1 January 2018 and during 2017, the Bank did not violate the mandatory standards established by the Bank of Russia, which are aimed at limiting the amount of credit risk.

On a regular basis the Bank performs an analysis of borrowers' financial position using the borrower's rating system. The Bank also regularly monitors collaterals and guarantees of organizations and individuals.

Market risk

Market risk is the risk of financial losses due to the changes in current (fair) value of financial instruments, as well as foreign exchange rates and (or) accounting prices for precious metals.

The objective of the Bank's market risk management is achieved through the system-wide, integrated approach that involves the following tasks:

- collection of current and objective information on the status and exposure to the market risk
- identification and analysis of the market risk arising in the course of the Bank's operations
- qualitative and quantitative market risk assessment (measurement)
- identification of correlations between the different types of risks to assess the impact of activities planned to limit one type of risk on the increase or decrease in the level of the other risks
- development of a market risk management system at the stage of a negative trend appearance, as well as a rapid and appropriate response system aimed at preventing market risk reaching the levels critical for the Bank (risk minimization).

In market risk managing the Bank follows the following principles:

- all operations conducted by the Bank in the money and financial markets are aimed at maintaining the Bank's core business and do not pursue speculative goals
- adequacy to the nature and size of the Bank's business
- making immediate adjustments in case of changes in the external and internal factors
- the possibility of a quantitative assessment of the relevant parameters
- continuous monitoring of the size of certain parameters
- performing risk assessment and preparation of appropriate management decisions by the same specially designated independent business unit
- feasibility of use
- availability of independent information flows on risks.

The following methods are used to achieve goals and objectives of the market risk management while complying with certain principles:

- system of boundary values (limits)
- system of authorities and decisions-making
- monitoring system for financial instruments
- controls system.

The main instrument used in strategic market risk management is the allocation of capital to cover it. The allocation is performed in accordance with risk appetite set for the Bank. The limit for capital used to cover market risk is approved by the Bank's Supervisory board. Any threats of possible violations of the approved limits are reported to the Management and Supervisory Boards of the Bank as soon as possible to take the adequate actions.

The target values of the capital used to cover market risk are supplemented by the operating measures that ensure that the risk is taken strictly within the prescribed limits and under careful control.

(expressed in thousands of Russian Roubles)

Quantitative indicators are defined in the internal document “Market risk assessment methodology”. The Bank applies the following models/methods to measure and assess the currency risk:

- assessment of an open-currency position
- VaR-analysis of a currency position
- Stress testing.

The following limits are used to manage the market risk:

- the required amount of capital to cover market risk, calculated in accordance with the Instruction of the Bank of Russia 180-I *On Mandatory Banking Standards*
- the cumulative long (short) open position in all foreign currencies, as a percentage of the Bank’s capital
- the amount of any long (short) open position in a given foreign currency, as well as the balancing position in Russian Roubles, as a percentage of the Bank’s capital
- the percentage share of the open positions in a given foreign currency in the amount of the Bank’s capital
- the VaR indicator (in % of capital).

Value-at-Risk (VaR) assessment methodology

Value-at-Risk (hereinafter – «VaR») – is a monetary measure of the maximum amount of expected losses for a given period of time determined with a given probability level. The VaR estimate is based on a performance of foreign exchange rates and instruments’ prices for the given historic time period.

The VaR provides an estimate of the market risk, the absolute maximum loss that can be expected from holding a financial instrument (or portfolio of instruments) over a fixed period of time (time horizon) under normal market conditions at a given confidence level.

The time horizon is measured as a number of working days. In order to estimate the amount of currency VaR, the Bank uses a time horizon of 250 working days.

The confidence interval used for VaR estimation is set at 95% and 99% (2 versions of estimation are carried out).

The forecasting horizon used for VaR estimation is set to 5 and 10 working days (2 versions of estimation are carried out).

The VAR model used is mainly based on historical simulation. The model derives plausible future scenarios based on historical market rate time series, taking into account inter-relationships between different markets and rates. Potential movements in market prices are determined with reference to market data from at least the last 12 months.

Although VAR is a valuable tool in measuring market risk exposures, it has a number of limitations, especially in less liquid markets as follows:

- the use of historical data as a basis for determining future events may not encompass all possible scenarios, particularly those that are of an extreme nature
- a 10-day holding period assumes that all positions can be liquidated or hedged within that period. This is considered to be a realistic assumption in almost all cases but may not be the case in situations in which there is severe market illiquidity for a prolonged period
- even the use of a 99% confidence level does not take into account losses that may occur beyond this level. There is a one percent probability that the loss could exceed the VAR estimate
- VAR is only calculated on the end-of-day balances and does not necessarily reflect exposures that may arise on positions during the trading day
- the VAR measure is dependent upon the position and the volatility of market prices. The VAR of an unchanged position reduces if market volatility declines and vice versa.

The VaR providing an estimate of losses relating to the portfolio of financial instruments is as follows:

	31 December 2017	**31 December 2016**
Foreign exchange risk	77	956
Interest rate risk	148 761	178 086

The Bank does not solely rely on its VAR calculations in its market risk measurement due to inherent risk of usage of VAR as described above. The limitations of the VAR methodology are recognized by supplementing VAR limits with other open position and sensitivity limit structures, including limits to address potential concentration risks within each trading portfolio, and gap analysis.

Interest risk

Interest risk (interest rate risk) is the risk of deterioration of Bank's financial position due to the decrease in the amount of equity, level of income, value of assets as a result of changes in interest rates on the market.

In accordance with the Business Development Strategy, the Bank does not carry out operations with the instrument of the trading book. Nevertheless, the main source of the Bank's profit is the interest margin.

The main sources of the interest risk are the following:

- mismatch of maturities of recognized and unrecognized assets and liabilities relating to instruments with a fixed interest rate
- mismatch of maturities of recognized and unrecognized assets and liabilities relating to instruments with a floating interest rate (interest rate repricing risk)
- changes in the configuration of the yield curve for long and short positions in financial instruments with one counterparty, creating a risk of loss as a result of excess of potential expenses over potential income at the close of these positions (yield curve risk)
- for financial instruments with a fixed interest rate, provided that their maturity is matched – the mismatch in the changes in the interest rates for funds borrowed and placed by the Bank; for financial instruments with a floating interest rate, provided that the floating interest rate is repriced with the same frequency – mismatch in the changes in interest rates (basis risk).

All operations conducted by the Bank in the money and financial markets are aimed at maintaining the Bank's core business and do not pursue speculative goals.

The Bank strives to maintain the interest rate at the level that does not threaten the financial stability of the Bank and concerns of its creditors and depositors, and thereby contributes to the stability and reliability of the Bank.

The main instrument used in strategic interest risk management is the allocation of capital to cover it. The allocation is performed in accordance with risk appetite set for the Bank. The limit for capital used to cover interest risk is approved by the Bank's Supervisory Board. Any threats of possible violations of the approved limits are reported to the Management and Supervisory Boards of the Bank as soon as possible to take the adequate actions. The target values of the capital used to cover interest risk are supplemented by the operating measures that ensure that the risk is taken strictly within the prescribed limits and under careful control.

The Bank applies the following models and methods for measurement and assessment:

- assessment of the level and dynamics of the interest margin and spread index
- GAP-model
- VaR method.

Interest margin is the difference between the interest income and the interest expense of the Bank. The margin is calculated both as an absolute value and as derived coefficients.

The absolute value of the margin can be calculated as the difference between the cumulative interest income and expense amount of the Bank, as well as between the interest income from given types of active transactions and the interest expense arising out of funding of these transactions.

The interest margin is determined in accordance with the Bank's Interest Policy, both across the Bank and at individual active transactions level. The risk exposure is estimated based on the dynamics of the margin. If the Bank sets the minimum acceptable interest margin, than the actual value of the coefficient may be compared to the minimum acceptable margin.

Spread is the difference between interest rates for active and passive transactions. The spread index demonstrates the range of variation of interest rates related to placements and funding.

GAP is the difference between the sum of long and short positions in financial instruments that are sensitive to changes in interest rates determined for each time interval. This value can be either positive or negative, and allows an analysis of the possible changes in the Bank's net interest income as a result of fluctuations in the interest rates. The larger the gap is the more is the Bank's exposure to the risk of losses from changes in the interest rates.

(expressed in thousands of Russian Roubles)

Excess of assets that are sensitive to the changes in interest rates over the liabilities that are sensitive to the changes in interest rates means that net interest income will increase as interest rates rise and decrease as the interest rates fall. The opposite situation means that the net interest income will increase as interest rates fall and decrease as the interest rates rise.

A financial instrument is sensitive to the changes in the interest rate if on the time horizon used to assess the interest risk, its value is expected to change based on the market dependent rate. Such assets, liabilities and unrecognized positions generate interest-sensitive margin.

Sensitive assets and liabilities include interbank loans and deposits, loans issued and attracted deposits with floating interest rates or with periodic interest repricing procedure in accordance with the contractual terms.

A financial instrument is not sensitive to the changes in the interest rate if either its value is expected change out of the time horizon, or the instrument is to be reinvested at a rate, that is not dependent on the market.

The VaR method is a quantitative assessment of the risk of loss for measurement of the interest rate risk. The standard deviation of changes in interest rates, profitability of financial instruments is calculated.

Average effective interest rates for interest bearing assets and liabilities as at 31 December 2017 and 2016 are provided in the table below. These interest rates are an approximation of the yields to maturity of these assets and liabilities.

	2017 Average effective interest rate, %			**2016 Average effective interest rate, %**		
	RUB	**USD**	**EUR**	**RUB**	**USD**	**EUR**
Interest bearing assets						
Nostro accounts with banks	0.01	0.03	0.40	0.21	0.01	0.00
Loans to banks	7.53	-	-	9.00	-	-
Loans to customers	13.38	9.22	-	14.95	7.12	-
Interest bearing liabilities						
Loans from banks	9.46	1.93	-	11.06	-	-
Other borrowings and customers' accounts	9.65	-	-	9.90	1.81	-
Bonds issued	9.06	-	-	10.75	-	-
Subordinated borrowings	8.46	-	-	8.46	-	-

Currency risk

Currency risk is the risk of losses due to unfavorable changes in foreign currency exchange rates and in open positions held by the Bank in foreign currencies.

The currency risk is primarily driven from changes in real value of the monetary obligation during a given time period.

Types of currency risk are as follows:

- operational – the possibility of loss or income deficiency from the transaction
- balance sheet (translational) – the mismatch between assets and liabilities, nominated in the foreign currencies.

All operations conducted by the Bank in the money and financial markets are aimed at maintaining the Bank's core business and do not pursue speculative goals.

The source of currency risk is the open currency position (hereinafter – "OCP"), which is a difference between the balances of assets and liabilities in a foreign currency (including unrecognized positions), that may lead to a possibility of additional profits or a risk of additional losses as a result of changes in the foreign exchange rates.

OCP may be:

- short – when the value of recognized and unrecognized liabilities exceeds the value of recognized and unrecognized assets in each currency
- long – when the value of recognized and unrecognized assets exceeds the value of recognized and unrecognized liabilities in each currency.

The Bank aims at maintaining the OCP value at a minimum level, i.e. at a level that does not threaten the financial solvency of the Bank and the concerns of its creditors and depositors, and thereby contributes to the stability and reliability of the Bank.

(expressed in thousands of Russian Roubles)

The Bank applies the following models and methods for measurement and assessment of currency risk:

- valuation of open currency position
- VaR-analysis of a currency position
- stress testing.

The OCP is assessed for compliance with the limits established by the ALCO (prior to their establishment – restrictions stated in accordance with the requirements of the current legislation). To quantify the currency risk the Bank uses the VaR methodology.

The following table shows the currency structure of assets and liabilities as at 31 December 2017:

	RUB	USD	EUR	Other currencies	Total
ASSETS					
Cash and cash equivalents	1 170 870	31 077	749	–	1 202 696
Mandatory reserve deposit with the Bank of Russia	238 908	–	–	–	238 908
Loans to banks	3 343 251	–	–	–	3 343 251
Loans to customers	51 572 094	6 371	–	–	51 578 465
Property, equipment and intangible assets	264 801	–	–	–	264 801
Current tax asset	25 328	–	–	–	25 328
Other assets	143 549	2 865	–	4 151	150 565
Total assets	**56 758 801**	**40 313**	**749**	**4 151**	**56 804 014**
LIABILITIES					
Loans from banks	19 899 539	57 841	–	–	19 957 380
Other borrowings and customers' accounts	15 520 032	–	–	–	15 520 032
Bonds issued	8 123 028	–	–	–	8 123 028
Subordinated borrowings	1 414 555	–	–	–	1 414 555
Deferred tax liability	140 027	–	–	–	140 027
Other liabilities	322 162	–	23	–	322 185
Total liabilities	**45 419 343**	**57 841**	**23**	**–**	**45 477 207**
Net position	**11 339 458**	**(17 528)**	**726**	**4 151**	**11 326 807**

The following table shows the currency structure of assets and liabilities as at 31 December 2016:

	RUB	USD	EUR	Other currencies	Total
ASSETS					
Cash and cash equivalents	723 392	32 679	235	–	756 306
Mandatory reserve deposit with the Bank of Russia	13 303	–	–	–	13 303
Loans to banks	3 400 836	–	–	–	3 400 836
Loans to customers	47 807 719	137 893	–	–	47 945 612
Property, equipment and intangible assets	223 448	–	–	–	223 448
Current tax asset	51 005	–	–	–	51 005
Other assets	174 444	825	–	852	176 121
Total assets	**52 394 147**	**171 397**	**235**	**852**	**52 566 631**
LIABILITIES					
Loans from banks	18 017 703	–	–	–	18 017 703
Other borrowings and customers' accounts	19 086 452	182 694	–	–	19 269 146
Bonds issued	3 094 886	–	–	–	3 094 886
Subordinated borrowings	1 414 393	–	–	–	1 414 393
Deferred tax liability	141 977	–	–	–	141 977
Other liabilities	260 684	–	21	–	260 705
Total liabilities	**42 016 095**	**182 694**	**21**	**–**	**42 198 810**
Net position	**10 378 052**	**(11 297)**	**214**	**852**	**10 367 821**

The analysis of an impact on the equity and net profit of the RUB exchange rate growth against other currencies is shown below. This analysis is based on foreign currency exchange rate movements that the Bank considers to be reasonably possible at the reporting date. The analysis assumes that all other variables, in particular interest rates, remain constant.

	31 December 2017		**31 December 2016**	
	Decrease, %	**Effect**	**Decrease, %**	**Effect**
Appreciation of USD against RUB	15%	2 816	30%	2 711
Appreciation of EUR against RUB	15%	3	30%	(51)

A weakening of the RUB against the above currencies would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

Operational risk

Operational risk is the risk of losses resulting from failures and deficiencies in Bank's internal operational procedures, malfunction of information and other systems or from impact of external events on operations of the Bank. Operational risk includes legal, model and counterparty risks.

A *legal risk* is the risk of losses as a result of:

- Bank's non-compliance with the requirements of regulatory legal acts and written contracts
- legal errors made in the course of operations (incorrect legal advice or preparation of documents, including when considering disputes in the judicial bodies)
- legal system inadequacy (inconsistency of legislation, lack of legal norms for regulating certain issues arising in the course of the Bank's activities)
- counterparties' violation of regulatory legal acts, as well as the terms of written contracts.

The Bank continuously monitors legal risks in order to take measures to maintain them at an acceptable level that does not threated the Bank's financial solvency, the concerns of its creditors, depositors, shareholders, employees, counterparties. Taking into account the recommendations of the Basel Committee, the Bank includes legal risks in the operational risks and provides general management systems for all types of operational risks.

To prevent or minimize the negative impact of unfavorable events on the Bank's processes, as well as to reduce (eliminate) possible losses, the Bank has introduced management tools for operational (including legal) risks recommended by the Basel Committee on Banking Supervision, such as: identification and collection of data on internal and external losses, their analysis and evaluation. All Bank's employees, as well as management bodies, when acting and/or taking decisions take into account the impact of operational (legal) risks.

The implementation, monitoring and control over operational (legal) risks are imposed on the Bank's collective bodies, the Risk Management Committee, as well as the Legal Department and the Financial Monitoring Department.

The *Model risk* is the risk of loss arising from the poor efficiency or inadequacy of the models used by the Bank.

The *Counterparty risk* is the risk of violation of business processes that may lead to losses or legislation violation by Bank as a result of a default of counterparties on their obligations to the Bank due to various reasons.

The *General operational risk* refers to operational risks not covered by model risk and legal risk.

The general operational counterparty risk was defined as significant for the Bank based on a procedure for determining the significant risks. Legal risk, model risk and counterparty risk based on a procedure for determining the significant risks are defined as other significant risks, which means that their realization in combination with the most significant risks may result in significant losses. These risks are recognized as relevant and are assessed within the general operational risk.

The significance of certain Bank's operational risk components is assessed within the work performed under the "Procedure for determining the significant risks".

The Bank's approved operational risk management policy provides prevention of the known risks and the identification of new operational risk arising in the course of the Bank's activities, as well as the development of procedures aimed at assessing, identifying and preventing of those risks.

Operational risk is inherent and extends both to the entire structure of the Bank as a whole and to all its activities, therefore operational risk management is based on such basic element as:

- improvement of business processes
- development of the bank's optimal structure
- innovation of control systems
- development of staff motivation schemes
- improvement of information technologies
- enhancing the business corporate culture
- set up a system that supports continues operations of the Bank.

The main instrument used in strategic operational risk management is the allocation of capital to cover it. The allocation is performed in accordance with risk appetite set for the Bank. The limit for capital used to cover operational risk is determined across the Bank.

Any threats of possible violations of the approved limits are reported to the Management and Supervisory Boards of the Bank as soon as possible to take the adequate actions.

The target values of the capital used to cover operational risk are supplemented by the operating measures that ensure that the risk is taken strictly within the prescribed limits and under careful control.

The Bank distinguishes the following methods used to minimize operational risks:

- **Risk awareness.** The management of all levels is responsible for managing the operational risk in the relevant field of activity. The banking operations are carried out in accordance with the rules and procedures approved by the Bank, within the established authorities, limits and restrictions. New banking operations are not allowed if regulations or appropriate decisions of the collegial bodies regulating the procedures for the transaction are not available.
- **"Four eyes principle".** Segregation of different functions, crosschecking, double control over the use of assets, a system of two signatures for the important documents, etc.
- **Segregation of duties.** The Bank builds adequate management structure that eliminates conflicts of interests: it is not allowed to combine powers (duties) to perform banking transactions with their processing and accounting, as well as to manage and control risks, including operational ones. This principle relates to both: individual performer, his subdivision and line of subordination, i.e. these functions are not allowed to be concentrated in one employee or within one unit, or within units subordinate to one manager. The following tools are used: additional authorization of operations, remote control, automatic checking and restriction, etc.
- **Control of operational risks.** The goal of the operational risks control is to obtain objective information about the level of operational risks, compliance with operational regulations and procedures, compliance with the established authorities and operational limits for assessing the effectiveness of the policies and the adequacy of the operational risk management system and their improvement. The control is performed on two levels: upper (managerial) and lower (operational). The management of Bank and its collective bodies regularly review reports on identified operational risks, the level of realized operational risks, facts, reasons and consequences of violations of established procedures, limits and restrictions, providing control at the upper (management) level. The authorized business units control operational risks at all individual stages of operations, implement procedures in accordance with the functions defined by the regulations on departments and regulatory documents of the Bank, which ensures control at the lower (operational) level. During identification of operational risks that are significant or systemic, the head of the relevant business unit in due order informs the Bank's management and the risk division. The operational risk control system is implemented in accordance with the principles defined by the Bank's internal regulatory documents and assumes the implementation of preliminary, current and follow-up controls over operational risks at all stages of transactions/procedures.
- **Use of information technologies**. To ensure timely detection, analysis, evaluation and control of operational risks, the Bank uses all available and accessible information systems and technologies. The specialized software requires preparation of the most detailed technical and user documentation.
- **Continuous improvement of the operational risk management system.** The Bank constantly improves the elements of the operational risk management system, including information systems, procedures and technologies based on the information on the realized risks and taking into account the strategic objectives, changes in the external environment, new international practices on managing of those risks.

Operational risk is assessed in accordance with the requirements of Regulation of Bank of Russia № 346-P dated 3 November 2009 *On the procedure for calculating operational risk*. When calculating the capital requirements for covering the operational risk, the Bank follows a standardized approach of the Instruction of the Bank of Russia 180-I *On Banks's Mandatory Ratios*.

As of 1 January 2018 and 2017 the Bank complied with the mandatory ratios established by the Bank of Russia.

Liquidity risk

Liquidity risk is the risk that the Bank becomes unable to finance its activities, i.e. to ensure the growth of assets and to settle its obligations as they fall due without incurring losses in the amount threatening the Bank's financial solvency. The liquidity risk includes the following significant components:

- *Short-term liquidity risk* is the risk of a mismatch between the amounts and dates of cash receipts and payments (cash inflows and outflows). The Bank has defined acceptable levels of risks in accordance with the "Risk and Capital Management Strategy".
- *Funding risk is* the risk of losses from entering into necessary funds raising transactions which are only possible at a less favorable terms. The risk relates to potential changes in the cost of funding (own and market credit spread), which affects the amount of the Bank's future income. The Bank manages the funding risk by calculating the level of capital adequacy within the framework of internal procedures for assessing capital adequacy. The Bank allocates capital for full coverage of funding risk. The most realistic scenario of funding risk development, considered by the Bank, is a case when the Bank loses access to the source of its cheapest funding – borrowings from TMFNL loans are subject to full early repayment of all tranches and, as a result, this part of the Bank's liabilities needs to be replaced by raising funds on an interbank loans market.

The main instrument used in strategic liquidity risk management is the allocation of capital to cover funding risk and assessment the Bank's acceptable stable liquidity position in respect of short-term liquidity risks. The allocation is performed in accordance with risk appetite set for the Bank.

The Bank has developed a liquidity management policy, which aims to provide liquidity control and timely full settlement of current liabilities. The liquidity management policy is reviewed and approved by the Supervisory Board of the Bank.

The Bank's Supervisory Board determines the liquidity management strategy across the Bank, including: approval of the Liquidity policy and the Regulation on the Asset and Liability Management Committee, hears the information on the liquidity position and provides recommendations on the general liquidity management strategy of the Bank.

The Bank's Management Board determines the liquidity management policy within the framework of the Bank's Development Strategy. Issues related to the liquidity management, if necessary, may be submitted for consideration of the meeting of the Bank's Management Board. In the event of a significant deterioration in the current or forecast liquidity situation, the Management Board may establish a special liquidity management regime, determine the list of operational measures, and determine the list of necessary measures.

The Asset and Liability Committee ("ALCO") takes responsible for enabling effective implementation of the liquidity management policies and procedures, as well as for the implementation of operational control of the liquidity position and for the implementation of liquidity management decisions made by the Management Board, including:

- as part of a process of medium- and long-term liquidity management approves the planned volumes and cost of attracting and allocating resources
- determines the range of the funding instruments used
- determines the methodology for quantifying the liquidity risk of the Bank
- decides on measures to mobilize liquid assets in the event of a liquidity shortage
- approves the methodology of the Bank's liquidity risk scenario analysis
- determines the composition and methodology of calculating quantitative indicators
- approves the criteria for classifying customers as large
- determines the maximum / minimum share of the liabilities attracted from non-residents
- performs other functions and has other authorities as defined in the Regulation on the Asset and Liability Committee.

ALCO and the Management Board of the Bank are called together in an emergency order in case of significant deterioration in the current or forecasted Bank's liquidity position.

The Treasury Department implements the ALCO decisions on liquidity management through the use of interbank, foreign exchange and other markets, attracting resources within the approved limits for the instruments of counterparties, and in accordance with the regulations of the Bank of Russia. The Treasury Department performs:

- continuous daily monitoring of the instant and current liquidity ratios
- regulation of the Bank's payment position and open currency positions
- daily consolidation of current information on cash flows from all the Bank's divisions, and setting the priority of payments in order to ensure compliance with the limits of mandatory liquidity ratios established by the Bank of Russia
- keeping the payment calendar by currencies for the nearest month to predict the excess or shortage of short-term liquidity
- informing the members of ALCO and the Management Board about the cases of significant deterioration of the Bank's liquidity or the current financial markets state
- comparison of the forecasted values of the liquidity ratios with the actual data in the financial statements using data provided by the Accounting, Reporting and Financial Control Department;
- together with the Credit Policy and Risk Management Department performs stress testing to determine the impact of stress factors on the liquidity of the Bank
- analysis, forecast and development of proposals on regulation of short-, medium- and long-term liquidity of the Bank together with the Financial Planning and Reporting Department and Credit Policy and Risk Management Department.

The Financial Planning and Reporting Department performs an analysis and planning of the short-, medium- and long-term liquidity, as well as develops mechanisms for monitoring deviations of the actual costs of maintaining liquidity from the planned one and provides recommendations for normalizing the liquidity of the Bank.

The accounting unit within Accounting, Reporting and Financial Control Department calculates on a daily basis the liquidity ratios established by the Bank of Russia, provides methodological support for modeling the impact of various scenarios and liquidity projections on ratios, and informs the Treasury Department and the Financial Planning and Reporting Department, if the critical internal limits on any ratio set by the Bank's internal policy are approached.

Credit Policy and Risk Management Department:

- develops and amends the Regulation on the Asset and Liability Committee
- develops proposals and recommendations on liquidity regulation
- controls compliance of the internal documents regulating the liquidity risk with the requirements of the Bank of Russia and shareholders
- submits to the ALCO an analysis of the liquidity values and the reasons for their violation
- controls compliance with the limits of the Bank's active operations
- develops proposals and recommendations for carrying out stress testing and determining the impact of the stress factors on the liquidity of the Bank
- provides disclosure to external users of the information on the actual liquidity risk level of as a part of the annual Bank's IFRS financial statements
- identifies and assesses the possible banking risks, including the liquidity risk
- standardizes and improves methods of liquidity risk analysis and management.

The liquidity management policy is based on the following principles:

- prediction of cash flows by main currencies and calculation of the required level of the liquid assets related to these cash flows
- maintaining a diversified structure of funding sources
- managing the borrowed funds concentration and structure
- development of plans for attracting financing through borrowed funds
- maintaining a portfolio of highly liquid assets that can be easily realized serving as a protective measure in case of an immediate liquidity gap
- development of reserve plans for maintaining liquidity and a given level of funding
- control over compliance of liquidity levels with the legislatively established ratios.

(expressed in thousands of Russian Roubles)

The following instruments are used to manage the liquidity risk:

- *Analysis of the liquidity gap by maturity* (GAP-analysis) is performed at least once a month and allows to identify the mismatch of assets and liabilities by maturity. The gap is the difference between assets and liabilities with the corresponding maturities before the remaining contractual repayment, combined into maturity groups.
- *Short-term liquidity forecast* (payment position) is performed on a daily basis and accounts for the most recent information, including information on planned issuance and repayments of loans to individuals and legal entities of the given maturity, on balances on correspondent accounts, on planned interbank credit operations, taking into account their maturity and the counterparty creditworthiness, on balances of the customers' accounts and planned account activity. The Bank takes cautious position when performing the analysis, i.e. doubtful assets are not taken into account when predicting the cash inflows, and liabilities with an indefinite maturity are accounted at the nearest possible date of claim.
- *Structuring and diversification of liabilities and funding sources* is used to reduce the risk of early liabilities claim and is performed if possible, preventively – at the stage of signing of credit documentation. The main instrument used to reduce this risk is the exclusion of contractual terms that provide for the creditor's ability to claim a debt before the maturity. Diversification of liabilities allows to reduce the Bank's dependence arising when assets are funded by one type of liability, and it implies a balance between raising funds from corporate clients and credit organizations, between funding instruments (term deposits, interbank loans, credit institutions, bonds, syndicated and subordinated loans, etc.)
- *Method of establishing ratios* is used to prevent violations of mandatory standards established by the Bank of Russia (N2, N3 and N4), as well as internal restrictions on liquidity deficit/surplus. The liquidity deficit/surplus is a cumulative difference between the amount of assets and liabilities with the remaining contractual maturity up to the specified number of days inclusive. The liquidity deficit cannot exceed 5%, 10% and 35% of total assets for the maturity groups "on demand and up to 7 days", up to 30 days and up to 1 year, respectively. The liquidity surplus cannot exceed 10%, 20% and 35% of total assets for the maturity groups "on demand and up to 7 days", up to 30 days and up to 1 year, respectively.

  In case of liquidity surplus, a strategy for placing excessive liquidity is being developed. At least 25% of the excessive liquidity is subject to placement in assets for up to 10 days on the correspondent accounts in the Bank of Russia and accounts of credit institutions, classified as the first risk group. Liquidity surplus can lead to a significant decrease in the Bank's profitability due to the low yield of highly liquid and liquid assets and/or high cost of borrowed resources.

  To set the limits, it is prohibited to maintain a level of excessive liquidity, resulting in decrease by more than 10% of the Bank's capital during 30 days, calculated in accordance with the Bank of Russia Regulation № 395-P *On the methodology for determining the amount of equity (capital) of credit institutions (Basel III)*. The effect on capital is calculated as 30/365 of the product of the weighted average interest rate for liabilities raised during the reporting month and the average liquidity excess. At the same time, the excess of liquidity is defined as the amounts on the correspondent accounts with the Bank of Russia and on accounts with credit institutions, regardless of their risk group, in amount exceeding 5% of the Bank's capital calculated in accordance with the Regulation.

  In case of a liquidity deficit, the responsible departments prepare the reports for consideration by the Bank's ALCO, including recommendations on liquidity ratios, interest rate risk, on increase in borrowings for a given term, and on exiting of certain operations to maintain credit lines open to the Bank for possible further use and/or recommendations to limit asset growth.

  As at 1 January 2018 and 2017, the Bank complied with the mandatory liquidity ratios set by the Bank of Russia. The following table shows the mandatory liquidity ratios calculated as at 1 January 2017 and 2016:

	Requirement	**1 January 2018**	**1 January 2017**
Instant liquidity ratio (N2)	Not less than 15%	189.5%	249.2%
Current liquidity ratio (N3)	Not less than 50%	209.4%	186.6%
Long-term liquidity ratio (N4)	Not more than 120%	74.4%	73.1%

- *Scenario analysis (stress testing)* provides the identification of alternative scenarios for the development of the market situation and their impact on the liquidity of the Bank, as well as the development of a behavioral strategy in case of an unexpected liquidity crisis in the Bank. The scenario analysis is performed at least quarterly. The following three main scenarios are considered:

- "Normal", i.e. operations under normal business activity. This is a basic scenario for forward-looking liquidity risk assessment.
- "Unfavorable", i.e. operations under a temporary liquidity shortage in the Bank. This scenario implies possible unfavorable developments for the Bank that may relate to emerging negative publicity of the Bank, the actions of certain Bank's creditors and borrowers, early redemption of liabilities, and delinquency of large assets.
- "Stress", i.e. operations in a general market crisis environment. Under this scenario of the liquidity analysis, the Bank's solvency is tested in the environment of sharp changes in the financial markets and absence of internal problems within the Bank caused by other factors. The following external factors on the Bank's activity are assumed: attraction of the interbank loans is impossible, there is a sharp drop in prices in the securities market, an increase in discounts on repurchase transactions at least twice from the current value.

A stress test is carried out in the form of a Report on the state of the Bank's forward-looking liquidity. Based on results of scenario analysis the Treasury develops liquidity recovery plans and proposals on hedging of prospective liquidity risk, and informs the ALCO.

The Treasury monitors the liquidity positions on a daily basis. Reports on liquidity rates are provided to the management at least once a month. Decisions on the liquidity management policy are made by the ALCO and executed by the Treasury. The results of the reports prepared by the ALCO are communicated to the management and the Supervisory Board of the Bank.

The Treasury together with The Financial Planning and Reporting Department and Credit Policy and Risk Management Department performs the following:

- prepares a detailed analysis of the structure of assets and liabilities by different breakdowns; at the same time, the main attention is paid to the forecasted outflow of the resources from the Bank for the next 3 month
- determines the types of business where it is possible to suspend the growth of assets, and provide practical steps in this direction
- forecasts the possibility of sale of assets, outlines the timing of sales and the amounts of proceeds
- develops the activities for dealing with the largest customers and counterparties
- specifies possible changes in the cost of the Bank's services (thus creating favorable conditions for the most important customers).

The employees and heads of the Bank's functions, whose decisions affect the liquidity level, perform operational control over compliance with liquidity management procedures. Timeliness of corrections of identified violations within the liquidity management process is controlled by the Bank's Management Board. To identify trends in improving or deteriorating of the Bank's liquidity position, the actual values of the liquidity ratios for the last reporting period are compared with the previous values for the last three month at least.

If the Bank is unable to raise funds on the interbank market, to maintain liquidity it uses a multicurrency credit line from Toyota Motor Finance (Netherlands) B.V. or other members of the international TOYOTA Group.

Making a decision to cover the liquidity deficit is the responsibility of the Bank's ALCO.

(expressed in thousands of Russian Roubles)

The following tables show the undiscounted cash flows on financial assets and liabilities and credit-related commitments on the basis of their earliest possible contractual maturity. The total gross inflow and outflow disclosed in the tables is the contractual, undiscounted cash flow on the financial asset, liability or commitment. Information about commitments is disclosed in note 23.

The position as at 31 December 2017 is as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	More than 1 year	Total gross amount	Carrying amount
Financial assets						
Cash and cash equivalents	1 202 696	–	–	–	1 202 696	1 202 696
Loans to banks	3 349 771	–	–	–	3 349 771	3 343 251
Loans to customers	5 268 782	6 871 184	14 413 411	38 040 535	64 593 912	51 578 465
Total financial assets	**9 821 249**	**6 871 184**	**14 413 411**	**38 040 535**	**69 146 379**	**56 124 412**
Financial liabilities						
Loans from banks	2 547 925	2 159 438	4 516 280	13 197 123	22 420 766	19 957 380
Other borrowings and customers' accounts	1 554 077	1 268 065	3 686 964	10 902 752	17 411 858	15 520 032
Bonds issued	–	3 161 692	403 603	5 807 205	9 372 500	8 123 028
Subordinated borrowings	–	579 735	55 040	905 040	1 539 815	1 414 555
Other liabilities	115 981	–	134 581	–	250 562	250 562
Total financial liabilities	**4 217 983**	**7 168 930**	**8 796 468**	**30 812 120**	**50 995 501**	**45 265 557**
Net position as at 31 December 2017	**5 603 266**	**(297 746)**	**5 616 943**	**7 228 415**	**18 150 878**	**10 858 855**
Credit related commitments	**400 000**	–	–	–	**400 000**	**400 000**

The position as at 31 December 2016 is as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	More than 1 year	Total gross amount	Carrying amount
Financial assets						
Cash and cash equivalents	756 306	–	–	–	756 306	756 306
Loans to banks	3 408 381	–	–	–	3 408 381	3 400 836
Loans to customers	6 125 042	8 707 950	13 705 331	31 989 240	60 527 563	47 945 612
Total financial assets	**10 289 729**	**8 707 950**	**13 705 331**	**31 989 240**	**64 692 250**	**52 102 754**
Financial liabilities						
Loans from banks	3 012 689	2 255 715	4 293 556	10 934 761	20 496 721	18 017 703
Other borrowings and customers' accounts	1 503 418	2 864 232	5 216 714	12 422 912	22 007 276	19 269 146
Bonds issued	–	161 692	161 692	3 485 075	3 808 459	3 094 886
Subordinated borrowings	–	29 696	88 601	1 539 815	1 658 112	1 414 393
Other liabilities	35 185	–	225 160	–	226 651	226 651
Total financial liabilities	**4 551 292**	**5 311 335**	**9 952 029**	**28 382 563**	**48 197 219**	**42 022 779**
Net position as at 31 December 2016	**5 738 437**	**3 396 615**	**3 753 302**	**3 606 677**	**16 495 031**	**10 079 975**
Credit related commitments	**332 976**	–	–	–	**332 976**	**332 976**

The analysis above is used by the Management to monitor current liquidity position of the Bank and to make related operational decisions.

Concentration risk

Concentration risk is the risk arising from the Bank's exposure to major risks, the realization of which may lead to significant losses that could pose a threat to the Bank's solvency and its ability of going concern.

The Bank determines the following forms of concentration risk:

- a significant amount of claims to one borrower or a group of borrowers
- a significant amount of investments in instruments of one type and instruments, the cost of which depends on changes in general factors
- credit claims to the counterparties in one economic segment or geographical zone, as well credit claims denominated in one currency
- credit claims to the counterparties whose financial results depend on one type of activity or sale of the same goods and services
- indirect exposure to the concentration risk arising from the Bank's implementation of measures to reduce credit risk (use of identical collateral, independent guarantees provided by one counterparty)
- dependence on certain types of income and on certain sources of liquidity.

The procedures for managing the concentration risk correspond to the Bank's business model, the complexity of transactions performed, and are a subject to review at least once a year. The Bank accounts for the concentration risk as a part of significant risk management procedures.

Business risk

Business risk is the risk of losses due to unfavorable changes in the general economic environment (for example, changes in consumers' behavior, intensity of competition, technological progress, etc.) and (or) due to general macroeconomic conditions. Business risk focuses on such potential effects during a one-year time horizon.

Business risk is considered as a residual risk, that is, a risk not yet mentioned among the above types of risk. Business risk leads to an unexpected decrease in income and (or) a negative deviation from the planned values.

The main components of a business risk:

- *Earnings risk* – the risk of losing the planned profit (part of profit) due to unforeseen changes in the general conditions of business and (or) the Bank's inability to adapt to such changing conditions. The main determinants of business risk are declining margins and (or) an increase in costs.
- *Reputational risk* – the risk of loss arising from the negative perception of the Bank by its members, counterparties, supervisors and other interested parties. The risk of loss of business reputation is critical for the Toyota brand that is why the entire Bank's policy is aimed at minimizing the risk. If the Bank suffers from a reputational strike, the losses will firstly come out with a decrease in sales.

In order to prevent the occurrence of reputational risk, the Bank has developed a mechanism that provides a set of effective actions aimed at identifying, assessing, monitoring and minimizing reputational risks.

Business risk assessment is carried out in accordance with the internal document that determines the order of units' interaction when forecasting the planned level of capital adequacy. Assuming the Bank will continue as going concern, when calculating capital adequacy, the Bank forms a buffer of capital to cover the business risk, which is deducted from the regulatory capital. There is no special limit on capital for the business risk. More important is the continuous monitoring of deviations between the realized profits and the planned ones.

Particular attention is paid to ensuring compliance with the Russian legislation, including anti-money laundering and terrorism financing, compliance of the Bank's activities with the good business practices and the principles of professional ethics, and ensuring the stability of the financial position.

The Bank's collective bodies, authorized Committees, and the Financial Monitoring Department are responsible for organizing, monitoring and controlling how the reputational risk is managed.

(expressed in thousands of Russian Roubles)

22. Capital management

The Bank of Russia sets and monitors capital requirements for the Bank.

The Bank defines as capital those items defined by statutory regulation as capital for credit institutions. The Bank calculates amount of capital in accordance with Provision of the Bank of Russia dated 28 December 2012 No 395-P *On Methodology of Calculation of own Funds (Capital) of the Credit Organizations (Basel III)* (Provision No 395-P).

The Bank maintains capital adequacy at the level appropriate to the nature and volume of its operations.

The Bank provides the territorial Bank of Russia that supervises the Bank with information on mandatory ratios in accordance with the set format. The Bank controls compliance with capital adequacy ratios on a daily basis.

Any cases of capital adequacy ratios approaching the limits set by the Bank of Russia and internal policies are communicated to the Supervisory and Management boards. As at 1 January 2018 and 2017, the Bank complied with the statutory capital ratios.

The information on statutory capital and its adequacy as at 1 January 2018 and 2017 is as follows:

	1 January 2018	1 January 2017
Base capital	9 443 824	8 584 871
Additional capital	-	-
Main capital	**9 443 824**	**8 584 871**
Supplementary capital	1 151 338	1 459 532
Own funds (capital)	**10 595 162**	**10 044 403**
Risk-weighted assets used to determine adequacy of basic and main capital	**57 399 139**	**53 883 180**
Risk-weighted assets used to determine adequacy of own funds (capital)	**57 402 707**	**53 890 797**
Basic capital ratio (N1.1)	16.5%	15.9%
Main capital ratio (N1.2)	16.5%	15.9%
Own funds (capital) ratio (N1.0)	18.5%	18.6%

As at 31 December 2017, the minimum levels of N1.1, N1.2 and N1.0 ratios are 4.5%, 6.0% and 8.0%, accordingly (2016: 4.5%, 6.0% and 8.0%, accordingly).

23. Credit related commitments

The Bank has outstanding commitments to extend loans. These commitments take the form of approved loans.

As at 31 December 2017, the contractual amounts of unused loan commitments totals RUB 400 000 thousand (2016: RUB 332 976 thousand). These total outstanding contractual commitments do not necessarily represent future cash requirements, as these commitments may expire or terminate without being funded. The majority of loan and credit line commitments do not represent an unconditional commitment by the Bank.

The Bank applies the same credit risk management policies and procedures when granting credit commitments, as it does for granting loans to customers.

(expressed in thousands of Russian Roubles)

24. Operating leases

The Bank doesn't have non-cancellable operating leases as lessee. Cancellable operating lease rentals as at 31 December 2017 and 2016 are payable as follows:

	2017	2016
Less than 1 year	120 576	161 804
Between 1 and 5 years	247 216	455 180
	367 792	**616 984**

25. Contingencies

Insurance

The insurance industry in the Russian Federation is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Bank doesn't have full coverage for its premises and equipment, business interruption, or third party liability in respect of property or environmental damage arising from accidents on its property or relating to operations. Until the Bank obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on operations and financial position.

Litigation

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

Taxation contingencies

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

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

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

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

(expressed in thousands of Russian Roubles)

26. Related party transactions

Control relationships. The Bank's parent company is Toyota Kreditbank GmbH (Germany). Non-controlling shareholder is Toyota Leasing GmbH. The party with ultimate control over the Bank is Toyota Financial Services Corporation (Japan).

Transactions with the members of the Supervisory and Management Boards. Total remuneration for 2017 and 2016 included in personnel expenses (note 8) is as follows:

	2017	2016
Wages and salaries	48 048	45 201
Bonuses	11 117	14 331
Apartment rent	3 076	2 585
Others	10 683	9 768
	72 924	**71 885**

Transactions with other related parties. Other related parties comprise affiliates and subsidiaries of the parent company.

The outstanding balances and average effective interest rates as at 31 December 2017 and related income and expenses for 2017 from transactions with other related parties are as follows:

	Parent company		Others		
	Carrying value	Average effective interest rate, %	Carrying value	Average effective interest rate, %	Total
Statement of financial position					
Other borrowings and customers' accounts					
- In Russian Roubles	-	-	14 168 434	9.65	**14 168 434**
Subordinated borrowings in Russian Roubles	-	-	1 414 555	8.46	**1 414 555**
Other assets					
- In Russian Roubles	-		4 707		**4 707**
- In EUR	-		4 108		**4 108**
Other liabilities					
- In Russian Roubles	-		2 031		**2 031**
- In USD	-		146		**146**
Statement of profit or loss and other comprehensive income					
Interest expense	-		(1 650 245)		**(1 650 245)**
Expenses on guarantee	-		(5 845)		**(5 845)**
Other income	-		26		**26**
Other general and administrative expenses	(33 181)		(29 025)		**(62 206)**

The outstanding balances and average effective interest rates as at 31 December 2016 and related income and expenses for 2016 from transactions with other related parties are as follows:

	Parent company		Others		
	Carrying value	Average effective interest rate, %	Carrying value	Average effective interest rate, %	Total
Statement of financial position					
Other borrowings and customers' accounts					
- In Russian Roubles	-	-	18 196 452	9.80	**18 196 452**
- In USD	-	-	182 693	1.81	**182 693**
Subordinated borrowings in Russian Roubles	-	-	1 414 393	8.46	**1 414 393**
Other assets in Russian Roubles	-	-	5 401		**5 401**
Other liabilities					
- In Russian Roubles	-	-	1 282		**1 282**
- In USD	-	-	125		**125**
Statement of profit or loss and other comprehensive income					
Interest expense	-		(1 731 955)		**(1 731 955)**
Expenses on guarantee	-		(4 139)		**(4 139)**
Other income	-		336		**336**
Other general and administrative expenses	(23 360)		(29 993)		**(53 353)**

(expressed in thousands of Russian Roubles)

27. Fair values of financial assets and liabilities

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

Fair value of financial assets is determined using valuation techniques. The objective of valuation techniques is to arrive at a fair value determination that reflects the price that would be received to sell the asset, or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

As at 31 December 2017 and 2016, the carrying amounts and fair values of financial assets and liabilities are as follows:

	2017		2016	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Cash and cash equivalents	1 202 696	1 202 696	756 306	756 306
Loans to banks	3 343 251	3 343 251	3 400 836	3 400 836
Loans to customers:				
Loans to auto dealers	7 441 614	7 613 885	10 436 407	10 322 291
Retail loans	44 136 851	45 246 844	37 509 205	37 503 480
	56 124 412	**57 406 676**	**52 102 754**	**51 982 913**
Loans from banks	19 957 380	20 616 268	18 017 703	17 851 796
Other borrowings and customers' accounts	15 520 032	16 048 330	19 269 146	19 195 300
Bonds issued	8 123 028	8 153 083	3 094 886	3 156 848
Subordinated borrowings	1 414 555	1 448 466	1 414 393	1 458 321
	45 014 995	**46 266 147**	**41 796 128**	**41 662 265**

The following assumptions are used by management to estimate the fair values of financial assets and liabilities:

- discount rates of 13.3% and 9.2% are used for discounting future cash flows in RUB and USD from retail loans to customers, which represent average interest rates for auto loans issued by the Bank in 2017 (2016: 15.5% and 9.1% accordingly, which represent average interest rates for auto loans issued by the Bank in 2016)
- discount rate of 11.2% (2016: 12.7%) and is estimated with reference to Mosprime non-deliverable forwards rates for respective tenor and currencies.
- discount rate for loans from banks, customers and subordinated borrowings is equal to Mosprime non-deliverable forwards rates for respective tenor and currencies.

The Bank measures fair values for financial instruments using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs, either directly (i.e., as prices) or indirectly (i.e., derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Fair value of loans to retail customers and loans from banks and customers is classified to the level 2. Fair value of loans to auto dealers and subordinated borrowings is classified to the level 3 of fair value hierarchy.

(expressed in thousands of Russian Roubles)

28. Analysis by segment

The Bank has two principal reporting segments – retail credit operations and financing of auto dealers. The segments are determined based on organizational structure and types of customers. A description of operations of each segment is provided below:

- ***retail credit operations*** comprise origination of auto loans to retail customers to facilitate acquisition of "Toyota" and "Lexus" vehicles, and maintenance of customers' current settlement accounts used for issuing and repaying of loans
- ***financing of auto dealers*** comprises issuing of credit lines and auto loans to official "Toyota" and "Lexus" auto dealers, and maintenance of current settlement accounts of auto dealers.

The Bank's operations are located in the Russian Federation and the Bank primarily issues loans to customers and auto dealers, being residents of the Russian Federation and conducting business in the Russian Federation. As the majority of revenues and assets are located in one geographic region (Russian Federation), the geographic analysis is not reported.

The Management measures segment results based on information about net interest margin and the level of assumed credit risk. The segment financial results comprise net interest and fee and commission income, and change in impairment allowance and provision under buy-back program. An average carrying amount of loans to customers, net of impairment allowance, is used as basis for allocation of funding sources and related interest expenses.

Segment information for each reportable segment as at 31 December 2017 and for 2017 is set out below:

	Retail credit operations	**Financing of auto dealers**	**Unallocated**	**Total**
Segment financial result				
Interest income	5 595 059	1 241 611	-	6 836 670
Interest expense	(3 288 982)	(720 187)	-	(4 009 169)
Net interest income	**2 306 077**	**521 424**	**-**	**2 827 501**
Fee and commission income	73 869	35 758	-	109 627
Fee and commission expense	(117 249)	-	-	(117 249)
Net fee and commission (expense) income	**(43 380)**	**35 758**	**-**	**(7 622)**
Other operating income	188 952	3 016	5 418	197 386
Charge for impairment losses	(301 707)	63 378	-	(238 329)
Provision under buy-back program	(364)	-	-	(364)
Total segment result	**2 149 578**	**623 576**	**5 418**	**2 778 572**
Segment assets				
Cash and cash equivalents	986 650	216 046	-	1 202 696
Loans to banks	2 742 686	600 565	-	3 343 251
Loans to customers	44 136 851	7 441 614	-	51 578 465
Total assets	**47 866 187**	**8 258 225**	**-**	**56 124 412**
Segment liabilities				
Loans from banks	16 372 334	3 585 046	-	19 957 380
Other borrowings and customers' accounts	12 732 089	2 787 943	-	15 520 032
Bonds issued	6 663 847	1 459 181	-	8 123 028
Subordinated borrowings	1 160 452	254 103	-	1 414 555
Total liabilities	**36 928 722**	**8 086 273**	**-**	**45 014 995**

(expressed in thousands of Russian Roubles)

Segment information for each reportable segment as at 31 December 2016 and for 2016 is set out below:

	Retail credit operations	Financing of auto dealers	Unallocated	Total
Segment financial result				
Interest income	5 252 789	1 421 644	-	6 674 433
Interest expense	(3 011 924)	(814 146)	-	(3 826 070)
Net interest income	**2 240 865**	**607 498**	**-**	**2 848 363**
Fee and commission income	372 114	38 480	-	410 594
Fee and commission expense	(332 464)	-	-	(332 464)
Net fee and commission income	**39 650**	**38 480**	**-**	**78 130**
Other operating income	96 559	1 603	13 322	111 484
Charge for impairment losses	(443 998)	205 367	-	(238 631)
Provision under buy-back program	6 561	-	-	6 561
Total segment result	**1 939 637**	**852 948**	**13 322**	**2 805 907**
Segment assets				
Cash and cash equivalents	589 849	166 457	-	756 306
Loans to banks	2 652 339	748 497	-	3 400 836
Loans to customers	37 509 205	10 436 407	-	47 945 612
Total assets	**40 751 393**	**11 351 361**	**-**	**52 102 754**
Segment liabilities				
Loans from banks	14 052 152	3 965 551	-	18 017 703
Other borrowings and customers' accounts	14 326 881	4 942 265	-	19 269 146
Bonds issued	2 413 727	681 159	-	3 094 886
Subordinated borrowings	1 103 096	311 297	-	1 414 393
Total liabilities	**31 895 856**	**9 900 272**	**-**	**41 796 128**

A reconciliation of segment financial result and profit before income tax is set out below:

	2017	2016
Total segment result	**2 778 572**	**2 805 907**
Net foreign exchange expense	(138)	(178)
Personnel expenses	(557 535)	(514 720)
Other general and administrative expenses	(996 256)	(871 829)
Profit before income tax	**1 224 643**	**1 419 180**

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President

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