



# ANNUAL REPORT 2017



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**Bernardino Bulla**

Chairman of the Board of Directors

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# Message from the Chairman of the Board of Directors

Dear Madam,  
Dear Sir,

For BancaStato, 2017 was a momentous year for a variety of reasons. The Institute saw a change in the chairmanship of the Board of Directors as the ordinary mandate of Fulvio Pelli, attorney at law, expired in June. Under his guidance, BancaStato experienced several significant changes, developing the approach and instruments needed to face the many present and future challenges in the banking sector. To him go the Institute's thanks.

This year, I have the pleasure of writing these lines of introduction to the Annual report as part of my new role as Chairman of the Board of Directors. As a Ticinese, I feel honoured to have been nominated by the State Council to fill this position and, since July, have tackled this new task with great enthusiasm and motivation. To my successor, Fabrizio Cieslakiewicz, I express my best wishes in his role as President of the Executive Board.

The year 2017 also proved significant as it was characterised by excellent economic and financial results. Mortgage loans increased by more than CHF 605 million to over CHF 8.8 billion. Net income further improved, reaching a CHF 48 million record high. The Bank's ownership thus benefitted from BancaStato's good overall performance as its profit transferred to the Canton exceeded CHF 36 million representing, we believe, a valuable source of income for the State.

These results were achieved within a consistently difficult context. Interest rates continue to remain at historically low levels despite a modest increase over the long term. The evolution of the Swiss GDP was weaker than expected and, in general, uncertainties about the economic situation have not lifted. However, as shown in this Annual Report, the Bank's business model continued to prove successful. Net revenues increased overall by CHF 3.3 million to CHF 181.5 million. Operating

expenses were also up, primarily because of an increase in expenses related to the implementation of the informatics system and to non-recurring costs pertaining to the staff pension fund. The operating result increased by CHF 3 million to CHF 72 million. The indexes of performance and efficiency have remained positive. New client assets amounted to CHF 559 million, for a total of CHF 11.3 billion (AuM).

As in the two previous years, BancaStato has made use of its excellent operating results to further bolster its equity while at the same time continuing to maintain growth in net profit. In 2015, CHF 22 million was allocated to the reserves for general banking risks. In 2016, this allocation amounted to CHF 24 million, and to CHF 26.1 million in 2017. This trend contributes to the strengthening of the Bank's capital base which is essential in order to allow it to rely on needed capital adequacy, and to enable it to maintain its lending policy for the benefit of the Canton's economy. The measure of the Bank's sound foundation (Tier 1 capital to Tier 2 capital) remains at a comfortable 15.7% whereas the Swiss Financial Market Supervisory Authority sets the minimum ratio for BancaStato at 12%.

Even though 2017 was not a favourable year for the asset management business in general, Axion SWISS Bank SA nevertheless achieved good results. Net profit was up by 16% reaching CHF 2.3 million despite a major goodwill depreciation from the acquisition of a portion of Société Générale Private Banking (Lugano-Svizzera) in March 2016 and from the investments connected to a new common informatics system with BancaStato which was implemented at the beginning of the year. The inflow of new client assets exceeded CHF 87 million.

Looking forward to the future, there will certainly be no shortage of challenges for BancaStato. These will not be times for



simply being content with the major results achieved thus far, but rather for pursuing efforts towards overall improvement and for reaching a better understanding of how to interpret a world which is, in many respects, in constant and increasingly rapid flux. It is not surprising, therefore, that one of the major upcoming challenges will be digitization, not only within the banking sector itself, but in the entire economy. I am certain that BancaStato will show the right grit to continually improve its delivery, maintaining high performance in service to Ticino and those who live in this Canton.

**Bernardino Bulla**

Chairman of the Board of Directors

# Corporate Governance

Corporate Governance is defined as a set of rules and relationships which dictate how an enterprise is managed: it is therefore intended to provide those essential elements to better understand how Banca dello Stato del Cantone Ticino is administered, as well as who is in charge of specific executive functions, and the basic principles which determine its operations.

## Introduction

Banca dello Stato del Cantone Ticino (BancaStato), in full respect of disclosure requirements laid down in Circular 2016/1 "Disclosure – banks" of the Swiss Financial Market Supervisory Authority (FINMA)<sup>1</sup> voluntarily publishes information on its corporate governance and draws reference from the outline proposed by the Directive on Information Relating to Corporate Governance issued by SIX Swiss Exchange on 13 December 2016<sup>2</sup>.

For information on risk management and monitoring measures implemented by the Group, refer to Section 5.3 of the Notes to the Consolidated Financial Statements.

All data herein are at 31 December 2017 or refer to the entire 2017 financial year, unless otherwise indicated.

## Corporate Name, Legal Status, Duration and Head Office

Banca dello Stato del Cantone Ticino, founded in 1915, is an autonomous institution operating under public law. The Republic and Canton of Ticino owns 100% of the Bank's equity. The Institution's statute is that of a cantonal bank, in accordance with the Swiss Federal Law on Banks and Savings Banks<sup>3</sup>.

The activities of the Bank are regulated by the Law on Banca dello Stato del Cantone Ticino dated 25 October 1988. The Bank is established with no time limit. Its head office is in Bellinzona<sup>4</sup>.

## Purpose and Activities

The purpose of BancaStato, as indicated in Art. 3 of the Law on Banca dello Stato del Cantone Ticino, is to promote the economic development of the Canton and to provide the public with opportunities for secure and remunerative investment of their

savings.

As stated in the above Law, the activities of the Bank extend to all operations of a full-service bank.

As illustrated in its Operating Rules and Regulations, the Bank's activities comprise:

1. acceptance of deposits in all forms allowed by the banking legislation;
2. granting of collateralised and non-collateralised loans and credits;
3. processing transactions with letters of credit and standby letters of credit, in particular in Commodity Trade Finance;
4. issuing guarantees, sureties and guarantee commitments;
5. securities trading for third parties and on own account;
6. trading in derivative financial instruments both for third parties and on own account;
7. issuing and participating in the issuance of shares, bonds and other securities, for both Swiss and foreign debtors;
8. spot or forward trading of currency and securities in foreign currency, precious metals and monetary market papers, both for third parties and on own account;
9. trading with professional banknote dealers as per Art. 2e of the FINMA Anti-Money Laundering Ordinance (ORD-FINMA; RS 955.033.0);
10. setup and distribution of investment funds in Switzerland and abroad, and the acceptance of mandates as a

<sup>1</sup> <https://www.finma.ch/it/~media/finma/dokumente/dokumentencenter/myfinma/rundschreiben/finma-rs-2016-01-01-01-2017.pdf?la=it>  
Any amendment or addition to this Circular will be communicated on [www.bancastato.ch](http://www.bancastato.ch), under "Media"

<sup>2</sup> [https://www.six-exchange-regulation.com/dam/downloads/regulation/admission-manual/directives/06\\_16-DCG\\_fr.pdf](https://www.six-exchange-regulation.com/dam/downloads/regulation/admission-manual/directives/06_16-DCG_fr.pdf)

<sup>3</sup> [http://www.admin.ch/ch/i/rs/c952\\_0.html](http://www.admin.ch/ch/i/rs/c952_0.html)

<sup>4</sup> <https://www3.ti.ch/CAN/Rleggi/public/index.php/raccolta-leggi/legge/id/1014/evidenzia/false/esplodi/false>

custodian and/or underwriter;

11. advisory, intermediation and asset management, as well as custody and administration of securities and valuables;
12. payment transaction processing in Switzerland and abroad;
13. carrying out the functions of an asset administrator;
14. providing treasury services;
15. providing custody and securities administration services, as well as safe deposit box rentals;
16. carrying out fiduciary transactions, in its own name, but on account and at the risk of customers;
17. issuing and placing of bonds, shares and other financial instruments, and participating in issues or financial operations of public or private corporations.

## Supervision

The Bank is subject to the supervision of the Swiss Financial Market Supervisory Authority (FINMA) pursuant to the provisions of the banking legislation<sup>5</sup>.

## 1. BANK STRUCTURE AND OWNERSHIP

### 1.1 Operational structure

#### 1.1.1 Group operational structure

BancaStato is a Group. As at 31 December 2017 the Bank held 100% of the share capital of the Lugano-based Axion SWISS Bank SA (nominal capital CHF 43 million)<sup>6</sup>. On the same date the Institution held a minority participation in Soave Asset Management Ltd., Lugano and Londinium Dac., Dublin. With this structure, BancaStato remains legally autonomous. As a Group, BancaStato has adopted special Group Regulations which lay down its overall organisational rules.

#### 1.1.2 Bank operational structure

The Heads of each Division, along with the President, form the Executive Board. The following business units report to the President of the Executive Board: Human Resources and Strategic Planning & Communications. The other business units are: Credit Management and Support, Markets and Private Banking, Retail and Corporate, and Financial and Operational Services.

### 1.2 Ownership

Banca dello Stato del Cantone Ticino is an autonomous institution with legal status under public law. The Republic and Canton of Ticino owns 100% of the Bank's equity.

### 1.3 Cross-shareholdings

The Bank does not have any cross-shareholdings.

## 2. CAPITAL STRUCTURE

### 2.1 Capital

By law, the State assigns the Bank an endowment capital and the Bank is authorized to issue participation certificates<sup>7</sup>. To this date, the Bank has not made use of the latter source of capital, and its capital solely consists of the endowment capital provided by the State, that is CHF 300 million. The interest paid out on endowment capital is fixed by the Bank's Board of Directors and by the State Council. A 5% interest was paid out on endowment capital in 2017.

### 2.2 Specifications concerning capital

Pursuant to Art. 6 of the Law on Banca dello Stato del Cantone Ticino, any increase in endowment capital must be authorized by the Grand Council (Cantonal Parliament). On 19 June 2017, the Grand Council approved a request for an increase of the endowment capital from CHF 240 million to CHF 500 million. This increase was granted in order to guarantee, in advance, adequate coverage in terms of capital adequacy in view of the Bank's growing business as well as in the event of more restrictive federal laws and regulations. This increase was

<sup>5</sup> <https://www.finma.ch/it/finma-public/isituti-persone-e-prodotti-autorizzati/>

<sup>6</sup> Although this is outside the reporting period, let it be reminded that, in 2016, Axion SWISS Bank SA finalized an agreement for the acquisition of a portion of client assets of the Ticino branch of Société Générale Private Banking (Lugano Svizzera) SA.

<sup>7</sup> <https://www3.ti.ch/CAN/RLeggi/public/index.php/raccolta-leggi/legge/id/1014/evidenzia/false/esplodi/false>

authorized through the transformation into endowment capital of perpetual subordinated loans for a total amount of CHF 140 million and through the authorization to increase capital by a further CHF 120 million<sup>8</sup>.

### **2.3 Changes in capital**

In consideration of the authorisation granted by the Grand Council (refer to Section 2.2), the State Council (Cantonal Government) increased the endowment capital to CHF 300 million (from CHF 240 million), following Government Resolution 5469 of 6 December 2017. This increase took effect on 31 December 2017.

In 2016, there were no changes in the endowment capital. In 2014, the endowment capital was increased from CHF 200 million to CHF 240 million. In 2013, it was increased from CHF 110 million to CHF 200 million, and in 2012 from CHF 100 million to CHF 110 million.

### **2.4 Shares and participation certificates**

The Bank's endowment capital is not divided up into shares. According to Art. 6 of the Law on Banca dello Stato del Cantone Ticino, the Institution is authorised to increase its participation capital by issuing participation certificates not exceeding 50% of its endowment capital.

As at 31 December 2017, just as at the end of 2016, there was no participation capital.

### **2.5 Bonus certificates**

The Law on Banca dello Stato del Cantone Ticino does not contemplate the issuing of bonus certificates.

### **2.6 Limitations on transferability and nominee registrations**

As the capital of Banca dello Stato del Cantone Ticino is not divided into shares, there is no relevant information to provide under this heading.

### **2.7 Convertible bonds and options**

BancaStato has not issued any convertible bonds, and there are no options on the Bank's equity. It is however important to mention the "old style" hybrid product – T2 loan (Tier 2 capital) with PONV, point of non-viability clause issued in 2011 for an amount of CHF 175 million and the AT 1 (Additional Tier 1) loan of CHF 80 million with PONV clause received from the Canton at the end of 2015. Although technically these loans are not convertible, in the event of the Bank's impending insolvency (PONV), these funds would contribute to its recovery through a credit reduction or a full conversion into capital (lenders' claims would be fully covered). For details, refer to the corresponding table of the Notes to the Group Financial Statements. With regard to loans received from the Canton, it must be mentioned that the CHF 60 million AT1 (Additional Tier 1) loan with PONV clause received at the end of 2014, was reimbursed at year-end. At the same time, and in conformity with the Grand Council authorisation of 19 June 2017, the Bank's endowment capital was increased by the same amount.

## **3. BOARD OF DIRECTORS**

### **3.1 Members of the Board of Directors and activities**

The Board of Directors exercises the ultimate responsibility for the management of the Bank and the supervision and control of the state of business. The Board is composed of seven members who must be Swiss citizens of which at least six must be domiciled in the Canton (Art. 19 of the Law on Banca dello Stato del Cantone Ticino).

Based on the provisions of Art. 20 of the Law on Banca dello Stato del Cantone Ticino, members of the State Council (Cantonal Government), government officials, magistrates of any type (except for justices of peace), Directors, administrators and employees of other credit institutions (with the exception of members of the Swiss National Bank governing bodies), cannot be appointed to the Board of Directors. Relatives and next of kin, spouses, registered partners or cohabiting partners, siblings or siblings-in-law, business partners and employees of the same company may not be members of the Board of Directors simultaneously.

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<sup>8</sup> [https://www4.ti.ch/user\\_librerie/php/GC/allegato.php?allid=115514](https://www4.ti.ch/user_librerie/php/GC/allegato.php?allid=115514)

The members of the Board of Directors fulfil the independence criteria described in FINMA Circular 2017/01<sup>9</sup> except for the Chairman who was, until 30 June 2017, President of the Executive Board. Given the above and, in agreement with the surveillance authority and the Statutory Auditors, the appointment of the Chairman was preceded by an internal reorganisation and a revision of the duties entrusted to the Bank's supervisory organs.

The members of the Board of Directors do not carry out operational functions and have not been members of the Statutory Auditors (previous or present).

Hereunder is a brief presentation of the members of the Board in office as at 31 December 2017<sup>10</sup>, their function, education, professional background and principal activities.

## **BERNARDINO BULLA**

### **Function**

Appointed Chairman of the Board of Directors on 15 March 2017, in charge since 1 July 2017. Born on 7 February 1957, Swiss. Chair of the Chairman's office.

### **Education and professional background**

Degree in Economics and Social Sciences from the University of Geneva in 1983. He started work for the Credit Department of BSI SA in Lugano in 1984. In 1997, he joined the Swiss Bank Society as Head of Private and Corporate Clients, then transferred to UBS SA as Head of International Clients and Trading within the Corporate Clients Division. At the end of 1998 he was responsible for corporate customers in Ticino at Credit Suisse, Lugano. He joined BancaStato on 1 October 2000 as a Member of the Executive Board and Head of the Corporate Clients Division. From 16 April 2007 to 31 December 2011, he was Head of the Risk Control Division. From January 2012 to June 2017 he was President of the Executive Board.

### **Other principal activities**

- » Chairman of the Board of Directors of Axion SWISS Bank SA, Lugano;
- » Chairman of the Foundation council of Fondazione del Centenario BancaStato, Bellinzona;
- » Member of the Board of Directors of Pizzarotti SA, Lugano.

## **CARLO DANZI**

### **Function**

Member of the Board of Directors, born on 24 February 1963, Swiss. On the Board of Directors since 10 July 2007, Secretary of the Board of Director from 1 October 2009 to 28 August 2017, when he took over the function of Deputy Chairman. Deputy Chairman of the Chairman's office and Member of the Projects Committee.

### **Education and professional background**

After the Lyceum and various language courses abroad, he worked for a pharmaceutical company in 1983, later becoming its owner in 1994. Since 1997 he has been the owner of a real estate management company based in Locarno.

### **Other principal activities**

- » Governing director of Fonte SA, Locarno;
- » Governing director of Laude SA, Locarno;
- » Sole member of the Carlo Danzi Foundation, Prato Leventina;
- » Sole member of the Ri di Foch Foundation, Prato Leventina.

## **MARCO FANTONI**

### **Function**

Member of the Board of Directors, born on 27 October 1957, Swiss. On the Board of Directors since 10 March 2009, Chairman of the Projects Committee.

### **Education and professional background**

He graduated in Commercial Sciences from the Cantonal Business School in Bellinzona and worked for Fidinam Fiduciaria SA, Lugano from 1977 to 1985. In 1987 he became the owner of Comafim SA, Lugano, a company active in the area of real estate promotion, administration of revenue buildings and condominiums and intermediation in houses, villas and apartments.

### **Other principal activities**

- » Member of the Board of Directors of the Carla and Bruno Fabbroni Foundation, Lugano.

<sup>9</sup> [https://www.finma.ch/it/~/\\_media/finma/dokumente/dokumentencenter/myfinma/rundschreiben/finma-rs-2017-01.pdf?la=it](https://www.finma.ch/it/~/_media/finma/dokumente/dokumentencenter/myfinma/rundschreiben/finma-rs-2017-01.pdf?la=it)

<sup>10</sup> The composition of the Board of Directors changed in 2017 as the mandates of Fulvio Pelli, attorney at law (Chairman) and Dr. Roberto Grassi (Deputy Chairman) expired at the end of June.

## **GIOVANNI JELMINI**

### **Function**

Member of the Board of Directors since 1 December 2011, born on 10 July 1962, Swiss. Member of the Audit and Risk Committee.

### **Education and professional background**

Degree in Law from the University of Fribourg, lawyer and public notary. Owner of the law and notary firm Jelmini from 1996 to 2009. Since 2010 co-owner of the law and notary firm Respini, Jelmini, Beretta Piccoli & Fornara. Grand Council Deputy from 1995 to 2011, he was a member of the Management Commission, Chairman of the Legislation Commission, Taxation Commission, Constitution and Political Rights Commission as well as of the Grand Council Public Mandate Control Commission of Banca dello Stato del Cantone Ticino. He was Cantonal President of Ticino's Popular Democratic Party from 2007 to 2015

### **Other principal activities**

- » Member of the Board of Directors of Axion SWISS Bank SA, Lugano;
- » Member of the Fondazione Cardiocentro Ticino, Lugano;
- » President of the Civic Philharmonic of Mendrisio.

## **MICHELE MORISOLI**

### **Function**

Member of the Board of Directors, born on 30 November 1966, Swiss. On the Board of Directors since 2 December 2008, member of the Audit and Risk Committee.

### **Education and professional background**

Master of Science (MSc) in Business Economics from the University of Lausanne in 1988. Worked for a leading banking institution in both Zurich and Ticino from 1988 to 1997. From 1997 to 2002, he was Administrative Director at the University of Lugano (USI). Until 31 December 2011 he was Director of the Regional Hospital of Bellinzona and Valleys, Director of the Oncology Institute of Southern Switzerland in Bellinzona and member of the General Management of the Cantonal Hospital Organisation (EOC – Ente Ospedaliero Cantonale). Since 1 January 2012 he has been the managing general agent of the insurance company Helvetia. Vice-president of the Liberal-Radical Party of Ticino since 2012.

## **Other principal activities**

- » President of the Casa dell'Accademia Foundation, Mendrisio;
- » Vice-president of the Associazione l'Ancora, a centre for drug addictions, Lugano.

## **RAOUL PAGLIA**

### **Function**

Member of the Board of Directors, born on 22 April 1967, Swiss. On the Board of Directors since 10 July 2012. Secretary of the Board of Directors since 28 August 2017 and Member of the Chairman's office. Member of the Audit and Risk Committee.

### **Education and professional background**

Master's degree from the "Ecole des Hautes Etudes Commerciales" of the University of Lausanne in 1993 and Certified EFFAS Financial Analyst and Portfolio Manager – AZEK in 1999. From 2003 to 2006, he was an expert examiner in financial operations for the Swiss Federal examinations in banking (Eidgenössische Bankfachprüfung). In February 2013, he obtained a Master's Degree in Advanced Studies in Tax Law from SUPSI. In 1993, he was employed by Banca del Gottardo in Lugano as a financial analyst. He started at BSI SA in 1996, and worked in the investment funds, institutional clients and stock markets departments. In 2011 he was responsible for stock markets for the Family Office Division (which later became Patrimony 1873) until June 2012, when he left the Institution. He is at present Managing Director and Member of the Board of Directors at AMCO Fiduciaria SA.

### **Other principal activities**

- » Member of the Board of Directors of Lugano Airport SA, Lugano;
- » Member of the Foundation Council of Perspectiva Joint Foundation, Basel;
- » Member of the Board of Directors of Swiss Investments SA, Lugano;
- » Member of the Board of Directors of SOAVE Asset Management Ltd., Lugano.

## LUCA SONCINI

### Function

Member of the Board of Directors, born on 18 May 1957, Swiss. On the Board of Directors since 11 October 2017. Member of the Projects Committee.

### Education and professional background

Degree in Economics from the University of Fribourg in 1981, subsequently researcher for the Economic Research Office of Canton Ticino. In 1982, he joined the daily newspaper *Corriere del Ticino* as chief editor for economic and financial news. During the 1980s, he also worked for the Italian Language Swiss Television in financial journalism. In 1987, he was employed by Banca del Gottardo and, in 1998, was appointed member of the Executive Board, Head of Private Banking. In 2007 he entered the PKB Privatbank group as a member of the Executive Board responsible for Finances and Risks. He was a member of the National Committee of the Swiss Bank Employers Association, the Executive Committee of the Ticino Bank Association, the Foundation Council of the Swiss Institute in Rome, the Board of Directors of Banca del Gottardo Italia SpA, Bergamo, the Board of Directors of Gestivalor-Gestione fondi SA, Lugano, the Board of Directors of Compagnia Finanziaria Mobiliare SIM SpA, Milan, and the Board of Directors of Banca Intermobiliare SpA, Turin.

### Other principal activities

- » Professor at the University of Lugano where he currently teaches a course titled "Banking Strategies" to students of the Master's programme in Banking and Finance, Lugano;
- » Member of the Foundation Council of the Swiss Finance Institute.

## 3.2 Other activities and vested interests of the members of the Board of Directors

This information is included in Section 3.1.

## 3.3 Elections and terms of office

The members of the Board of Directors are appointed by the State Council. Their education, competence and professional history are decisive criteria for their appointment. They remain in office for 3 years, until 30 June. Retiring members may be re-elected. On an annual basis, the State Council renews two or two and three mandates respectively. The maximum term of office is 12 years (Articles 21 and 22 of the Law on Banca dello Stato del Cantone Ticino).

The dates of election and terms of office for the present members of the Board of Directors are as follows:

- » Bernardino Bulla, Chairman: 1 July 2017 / 30 June 2020,
- » Carlo Danzi, Deputy Chairman: 10 July 2007 / 30 June 2019,
- » Marco Fantoni: 10 March 2009 / 30 June 2018,
- » Giovanni Jelmini: 1 December 2011 / 30 June 2019,
- » Michele Morisoli: 2 December 2008 / 30 June 2020,
- » Raoul Paglia: 10 July 2012 / 30 June 2018,
- » Luca Soncini: 16 October 2017 / 30 June 2020.

## 3.4 Internal organisational structure

The Board of Directors elects among its members the Chairman, the Deputy Chairman and the Secretary, who together form the Chairman's Office.

The Board of Directors reaches a quorum when at least five of its members are present. Decisions are determined by a simple majority of those present, and abstention is not permitted.

In principle, the President of the Executive Board attends the meetings in an advisory capacity. With prior agreement from the Chairman of the Board of Directors, he may invite members of the Executive Board to the meetings for the presentation of specific points on the agenda. Every member of the Board of Directors must inform the other members of possible conflicts of interest and/or conflicts in personal business or that of relatives, and may not in those circumstances attend or take part in deliberations or vote on the subject matter. Minutes are taken at each meeting.

The Board of Directors has defined its own committees, which are described below. The organisation, functioning and competences of the committees are illustrated and set out in specific rules and regulations.

Every member of the Board of Directors is entitled to obtain, under absolute observance of professional secrecy (Art. 11 of the Law on Banca dello Stato del Cantone Ticino), information and details on all Bank business. The members of the committees of the Board of Directors have, within the framework of their mandate, an unlimited right to information on and consultation of Bank documents. The Executive Board and the Internal Auditors must provide the committees of the Board of Directors with all information they require.

In 2017, the Board of Directors convened 14 times. The meetings of the Board of Directors and its committees lasted between two and a half and four and a half hours.

### 3.5 Areas of responsibility

The Board of Directors exercises the ultimate responsibility for the management of the Bank, as well as the supervision and control over the state of business. Pursuant to applicable law, regulatory, organisational, strategic and financial responsibilities, as well as supervision and control, lie with the Board of Directors.

Some of its tasks, as defined by Art. 24 of the Law on Banca dello Stato del Cantone Ticino and Art. 11 of the Operating Rules and Regulations are listed by category hereunder:

#### *Regulatory duties*

- establishing the Bank's regulatory provisions;
- laying down and updating, on a regular basis, the operating rules and the Organisation and Risk Management Regulations, and other regulations;
- drawing up a formal document on the public mandate in view of defining the general and specific objectives which are to be met in the medium term by the Bank in favour of the development of the cantonal economy, specifying the instruments to be used to this end and priorities;
- issuing Staff Rules and Regulations upon prior consultation with personnel.

#### *Organisational duties*

- establishment of the Bank's organisation;
- definition of the Bank's organisational chart;
- allocation of appropriate resources within the Bank in terms of personnel, infrastructure and IT;
- appointment, suspension, removal or dismissal of the President of the Executive Board, members of the Executive Board, members of Management, Chief Internal Auditor, Deputy Chief Internal Auditor and the Compliance Officer as well as their periodic assessment,

and planning their succession accordingly;

- compensation and adoption of disciplinary measures as regards the Executive Board, the Chief Auditor and the Deputy Chief Auditor;
- organisation of accounting, controlling and financial planning;
- establishment and closing of branches and agencies;
- appointment and dismissal of External Auditors;
- granting or revoking power to sign as laid down in Art. 22 and 23 of the Operating Rules and Regulations;
- authorisation to assume mandates as corporate or foundation bodies on the part of all Bank staff;
- authorisation to operate in new sectors;
- approval of tasks and objectives of each division;
- decision to appear in court and initiate legal proceedings, with power to delegate;
- appointment of the Chairs of the Committees of the Board of Directors.

#### *Strategic and financial duties*

- approval of the Bank's financial plans and strategic guidelines laid down in the strategic planning document;
- review and approval of budgets, accounts, semi-annual and annual financial reports;
- approval of capital planning and liquidity planning;
- definition of the staff and remuneration policies;
- review and approval of the Annual Social and Environmental Report and of the section on Corporate Governance of the Annual Report;
- decision on the issuance of participation certificates as per special regulations and the annual setting of the base dividend on participation capital;
- decision-making, upon notice from the Executive Board, on requests for loans, credits or advances and on operations which engage Bank funds or its pecuniary

responsibility and which are not part of delegated responsibilities as laid down in the Operating Rules and Regulations;

- approval of loans to the members of the Executive Board and the Chief Internal Auditor;
- ratification of loans granted to members of the Board of Directors by the Executive Board or by its subordinate offices within the framework of their delegated responsibilities;
- decision-making on the acquisition and disposal of participations exceeding CHF 2 million, or 15% of the subsidiary's capital, within the limits set by Art.14 of the Law on Banca dello Stato del Cantone Ticino;
- fixation, in agreement with the State Council, of the interest rate on the endowment capital;
- providing the State Council by 31 March of each year with the annual report, financial statements, proposal for appropriation of available earnings and Statutory Auditors' report;
- providing the Grand Council by 31 March of each year with the Auditors' report in compliance with Art. 37a of the Law on Banca dello Stato del Cantone Ticino;
- establishment of reference rates and oversight to ensure that the individual rates set by the Executive Board comply with Art.3 of the Law on Banca dello Stato del Cantone Ticino;
- reporting to the FINMA in the event that capital or liquidity requirements are not met, or maximum limits on major risks have been exceeded;
- current operating expenses and investments in infrastructure which are not specifically delegated to the Executive Board.

#### *Supervision and control duties*

- determining the control procedures to undertake in line with current applicable external regulatory provisions;
- oversight on compliance with banking regulatory

provisions with respect to risks, in particular the control of major risks as per Ordinance on Capital Adequacy and Risk Diversification for Banks and Securities Traders (CAO, RS 952.03) and the requirements of the Ordinance on Liquidity (OLiq, RS 952.06),

- supervision of the work of the Executive Board, including assessment of the Executive Board in terms of meeting its objectives and its work procedures;
- supervision of the work performed by the Internal Auditors and the Legal and Compliance Office;
- annual appraisal and assessment of the Bank's framework strategy for risk management, implementing any necessary adjustments, as well as undertaking its own risk analysis;
- review of the reports of the External Auditors and the Internal Auditors;
- analysis of the summary prepared by the Head of Credit Management and Support of the results of various reports on activities and risk evaluation.

Moreover, the Board of Directors makes decisions, in accordance with Art. 24 of the Law on Banca dello Stato del Cantone Ticino, on any other matter that the said Law or the Bank's Rules and Regulations do not explicitly assign to another Bank body or authority.

With respect to consolidated supervision, the Board of Directors exercises its competences on the basis of the Group Rules and Regulations which is drawn upon the principles mentioned above (Art. 24 of the Law on Banca dello Stato del Cantone Ticino and Art. 11 of the Operating Rules and Regulations).

In compliance with Art. 25 of the Law on Banca dello Stato del Cantone Ticino, the Board of Directors may delegate part of its duties, to the exclusion of those inalienable on the analogy of Art. 716a of the Swiss Code of Obligations<sup>11</sup>, to permanent or ad hoc committees composed of members of the Board of Directors or to the Executive Board.

As a rule, the Committees do not have any decision-making authority; they draw up notices to the Board of Directors on matters relating to their own charter. Specific decisional authority may be attributed by the Board of Directors.

<sup>11</sup> <https://www.admin.ch/opc/it/classified-compilation/19110009/index.html>

Minutes are taken at every meeting of the Committees.

With respect to the delegation of duties to the Executive Board, refer to the corresponding paragraph under Executive Board.

The functions and organisation of the Chairman's Office and the Board of Directors' Committees as at the end of 2017 are described hereunder.

As laid down in internal regulatory provisions, at Group level, the activities of the Committees of the Board of Directors also comprise all issues entrusted for the Group to BancaStato's Board of Directors.

### **Chairman's Office**

The Chairman's Office represents the Bank vis-à-vis its owner as well as political institutions and public opinion.

The Chairman's Office is composed of the Chairman, Bernardino Bulla, the Deputy Chairman, Carlo Danzi and the Secretary, Raoul Paglia. In 2017, the Chairman's Office convened once.

### **Audit and Risk Committee<sup>12</sup>**

The Audit and Risk Committee of the Board of Directors deals with issues relating to financial matters, internal control systems and risk management, as well as external and internal audits.

With respect to financial matters, the Committee examines the issues and draws up recommendations for the Board of Directors regarding the following:

- decision on accounting principles to be adopted for the preparation of accounts;
- approval of annual and semi-annual financial statements,
- approval of the budget;
- approval of capital and liquidity planning;
- approval of expenses and overrun expenditures for matters which fall within the authority of the Board of Directors;
- organisation of accounting, reporting and financial planning;

- discussion with the member of the Executive Board responsible for Finances and Accounting, as well as with the Statutory Auditors and the Internal Auditors on financial reporting and integrity of financial closures;
- definition of the policy in matters of staff and remuneration.

As regards the internal control system and risk management, it examines and submits notices to the Board of Directors on the following:

- functioning, efficiency and results of the internal control system;
- strategic decisions relative to risk management and, at least once a year, an evaluation of the framework strategy;
- functioning, methodologies, efficiency and results of the risk management system;
- procedures to ensure that all risks incurred by the Bank are duly identified, assessed, monitored and controlled;
- compliance with current or upcoming banking rules and regulations within the banking business;
- system for monitoring irregularities or recommendations issued by the audit authorities;
- adequacy of the internal control and risk management system with regard to the Bank's strategic decision-making;
- reports of the Executive Board on risk management;
- matters within the competence of the Board of Directors listed in the appropriate Organisation and Risk Management Regulations;
- reports on the risk-assessment activities of the Legal and Compliance and Human Resources offices, as well as Competence Centres and the organizational units for Risk Management, Group Internal Control and Security;
- rules and regulations within the competence of the Board of Directors.

<sup>12</sup> The Strategic Committee was dissolved in 2017. Its duties were integrated with the activities of the Audit and Risk Committee.

The Audit and Risk Committee examines and submits notices to the Board of Directors also as regards the following:

- supervision of specific regulatory and organizational competences which are entrusted to the Board of Directors;
- acquisition and divestment of participations which fall within the responsibility of the Board of Directors;
- proposals for expanding the Bank's business scope.

As for internal and external audits, the Committee draws up further recommendations on specific matters, and brings them to the attention of the Board of Directors. The Audit and Risk Committee of the Board of Directors is composed of the Chairman, Michele Morisoli, and Giovanni Jelmini and Raoul Paglia, members. In 2017 the Committee convened nine times.

### **Projects Committee**

The Projects Committee examines and draws up notices to the Board of Directors on:

- planning, implementation, management and control methods, budgets and observance thereof, work progress, reasons pertaining to planning variations, future impacts and other possible aspects of current projects;
- planning, budgets, implementation, management and control methods, future impact and other possible aspects relating to projects which the Bank may consider;
- investments which fall within the authority of the Board of Directors.

The Projects Committee is composed of the Chairman, Marco Fantoni and Carlo Danzi and Luca Soncini, members. In 2017 the Committee met twice.

### **3.6 Information and control instruments vis-à-vis the Executive Board**

In line with the Operating Rules and Regulations, the President of the Executive Board reports to the Board of Directors:

*On a monthly basis*

- the balance sheet and income statements;
- information on the Bank's liquidity, equity, and major risks;
- the situation as regards risks and information on the functioning, effectiveness and results of the internal control system.

*On a semi-annual basis*

- the consolidated balance sheet and consolidated income statement;
- information on measures to be implemented in order to close loopholes and on the progress of the implementation of recommendations resulting from the internal and external audits.

*On an annual basis*

- strategic planning;
- budgets, financial statements and annual reports;
- information regarding the general state of business with respect to objectives and strategies set by the Board of Directors and the general situation at the Bank;
- the Social and Environmental Report as well as the chapter of the Annual Report on Corporate Governance;
- assessments of amendments to regulations on the competences of the Board of Directors;
- confirmation of adequate allocation of resources both in terms of personnel and equipment;
- a report on the activities and risk evaluation of the Legal and Compliance Office, the Human Resources Department, the Competence Centres, and the organizational units of Risk Management, Internal Group Controls and Security;
- summary of the results of various reports mentioned in the above paragraph.

As deemed necessary, other documents or data may be requested.

The fundamental principles of information flows have been set also for the Group. The Bank has External Auditors, in conformity with current banking legislation as well as Internal Auditors (refer to Section 8.1). The Internal Auditors' Office is independent of the Executive Board and was composed at the end of 2017 of five staff, including the Chief Auditor (Mr. Gabriele Guglielmini, Chartered Accountant – Federal Accounting Diploma). The Chairman of the Audit and Risk Committee of the Board of Directors acts as the Chief Internal Auditor's direct superior and oversees his activity.

The audit is planned in agreement with the Board of Directors. The latter may assign specific checks, investigations or controls to the Internal Auditors. Details pertaining to the organisation, functions and duties of the Internal Auditors are laid down by the Board of Directors in special regulations. The internal audit provides important bases for decision-making to evaluate and verify whether the Institute can rely on an appropriate and efficient internal control system. It conducts at least annually a comprehensive risk assessment and plans its activities for the following audit period. The personnel involved in internal auditing may not take part in Bank operational processes.

The members of the Board of Directors receive all reports relating to ordinary audits. These documents comprise also the stance of the Executive Board on the recommendations formulated by the Internal Auditors. The Internal Audit reports are discussed by the Internal Auditors with the Audit and Risk Committee of the Board of Directors and the Board of Directors. The Internal Auditors satisfy the requirements of the Institute of Internal Auditing, Switzerland.

#### **4. EXECUTIVE BOARD**

The Board of Directors may delegate part of its functions relating to business management, to the exclusion of those inalienable on the analogy of Art. 716a of the Swiss Code of Obligations, to the Executive Board.

The functions of the Executive Board are listed in detail in Art. 15 of the Operating Rules and Regulations, and are the following:

#### *Regulatory duties*

- implementing the regulatory provisions and recommendations of the supervisory authority and surveillance bodies, internal and professional guidelines, and oversight on compliance of the same;
- issuing specific regulations, guidelines and appropriate orders as required for the performance of banking activities;
- implementing the provisions as laid down in the public mandate document;
- implementing the measures set out in the Staff Rules and Regulations;
- issuing a code of conduct and laying down the sanctions in case of non-compliance.

#### *Management and organisational duties*

- implementation of the Bank's organisation;
- implementation of the Bank's detailed organizational chart;
- development of the Bank's strategic planning and implementation of the measures envisaged in the same based on decisions of the Board of Directors;
- organisation of financial management controls;
- recruitment, compensation, appointment and disciplinary measures, dismissals, as well as direction and supervision of staff other than those falling within the authority of the Board of Directors;
- preparation of the documents pertaining to matters to be submitted to the Board of Directors;
- membership in trade associations;
- decision to appear in court and initiate legal proceedings, as delegated;
- apprising the Board of Directors on the Bank's business development and on its economic and financial state;
- definition of the duties and targets in each division;
- provision of an adequate technological infrastructure.

### *Financial duties*

- preparation of budgets, semi-annual and annual financial statements;
- drawing up of the Social and Environmental Reports and of the section of the Annual Report on Corporate Governance;
- approval of monthly accounts to be submitted to the Board of Directors;
- implementation of the decisions taken by the Board of Directors with regard to loan requests, credits and advances on operations which engage Bank funds or pecuniary responsibility, and which are not included in delegated responsibilities as outlined in the Operating Rules and Regulations;
- decision on risk-incurring and on investments and expenditure, within the limits of the relevant Organisation and Risk Management Regulations;
- decision on the issuance of bonds or other third-party asset gathering;
- determination of individual interest rates, in accordance with the provisions of Art. 3 of the Law on Banca dello Stato del Cantone Ticino;
- preparation of capital planning and liquidity planning;
- reporting to the Board of Directors in the event capital requirements are not met or of major risks or liquidity;
- decision-making on the acquisition and disposal of participations not exceeding 15% of the subsidiary's capital or CHF 2 million.

### *Supervision and control duties*

- implementation of the control procedures based on applicable external regulatory provisions;
- implementation of the provisions envisaged in the Organisation and Risk Management Regulations and the proposals for update to be submitted to the Board of Directors;

- supervision on risks incurred and adequacy of allocated capital;
- preparation of the records for the Public Mandate Control Commission of the Cantonal Parliament;
- establishing an evaluation with respect to its own work procedures and the meeting of its objectives.

### *Credit duties*

- decisions related to credit business on the basis of delegated competencies defined by the Board of Directors.

With respect to the Group's operational management, it is important to note that the Executive Board exercises its own competences based on the Group Regulations.

The activities of the Executive Board are supported by the business units of the Executive Management, as well as by specific committees of the Executive Board, whose principal responsibilities are summarised below.

These committees carry out their own functions also for specific issues pertaining to the Group.

### **Risk Committee**

The Risk Committee is responsible for ensuring adequate supervision of overall risk and, in particular, operational risks. The duties assigned to this Committee are to develop risk profiles within the framework of thresholds set by the Board of Directors, to ratify the individual operational losses up to the threshold described in the Committee's regulations, and the provision of infrastructure and adequate resources for the control and supervision of risks (including aspects related to personnel and outsourced activities).

The Risk Committee is chaired by the President of the Executive Board. Its Deputy Chairman is the Head of Financial and Operational Services.

## Credit Risk Committee

The Credit Risk Committee is responsible for managing the credit risk with the aim of optimising its administration. Within the framework of the competencies assigned to it, the Credit Risk Committee decides on loan applications (loan granting, extension, renewal, increase). It also proceeds to a preliminary examination of and submits prior notice on all matters which are brought to the attention of the Board of Directors for information or debate.

The Chairman of the Credit Risk Committee is the Head of Credit Management and Support. The Deputy Chairman is the Head of the Retail and Corporate Clients Division.

## ALCO (Assets & Liabilities Committee)

Within the framework of assignments entrusted to it, the ALCO is responsible for the market risk, including liquidity risk, on all Bank portfolios in view of optimising the management of this risk based on the Bank's strategy and budget. More specifically, this Committee manages rate and currency risk exposure on the balance sheet (as regards both benefits and economic value), overall liquidity, positions in the financial investment portfolio, and exposure to market risk derived from trading activities.

This Committee is chaired by the Head of Markets and Private Banking. The Deputy Chairman is the President of the Executive Board.

## 4.1 Members of the Executive Board

The Executive Board comprises the President of the Executive Board and members who are all Heads of Divisions. The members' term is indefinite, and they retire three years earlier than the standard age of retirement, provided that their nomination occurred at least 10 years before the standard retirement age. No member of the Executive Board was ever a member of the Bank's Board of Directors or worked for the Internal Auditors (past or present).

Following is a short introduction to the five members in office as at 31 December 2017 along with their functions on the Executive Board, their educational background, their professional record of accomplishments and their other activities<sup>13</sup>.

## FABRIZIO CIESLAKIEWICZ

### Function

Appointed President of the Executive Board on 15 March 2017, effective on 1 July 2017. Member of the Executive Board since 1 August 2008; born on 4 September 1970, Swiss.

### Education and professional background

Degree in Political Economics from the University of Lausanne in 1993. In 1994 he was employed by UBS SA as a member of a post-graduate team for corporate clients in the Ticino area. In the following year, he became a business consultant for corporate clients and member of the managerial staff. From the end of 1997 to the beginning of 2000 he was Head of the General Secretariat for the Liberal Radical Party of Ticino. He began his employment at BancaStato on 19 June 2000 as Deputy Manager of the Biasca Agency. On 31 December 2001, he was appointed Member of the Management and assumed the position of Regional Head and Head of the Corporate Clients Division for the Bellinzona Area. On 1 August 2008 he was appointed Member of the Executive Board and took over the position of Head of Retail and Corporate Clients. On 1 July 2017 he assumed the role of President of the Executive Board while continuing to maintain, on an interim basis, the responsibility for the Retail and Corporate Division until 1 December 2017.

### Other activities

- » Deputy Chairman of the Foundation Council of the Fondazione di Previdenza Risparmio 3 of Banca dello Stato del Cantone Ticino;
- » Member of the Board of Directors of the Association of Swiss Cantonal Banks, Basel;
- » Member of the Executive Committee of the Ticino Bankers' Association;
- » Member of the Foundation Council of the Center for Banking Studies;
- » Member of the Board of the Carlo and Albina Cavargna Foundation;
- » Member of the Board of Governors of the Ticino Cancer League.

<sup>13</sup> At the beginning of July 2017, Bernardino Bulla, then President of the Executive Board, assumed the chair of the Board of Directors, taking over from attorney at law Fulvio Pelli, whose mandate expired.

## **DANIELE ALBISETTI**

### **Function**

Member of the Executive Board since 1 April 2014, born on 28 October 1962, Swiss.

### **Education and professional background**

Degree in Economics with a major in Corporate Management from the University of Lausanne in 1985. He began his professional career in the internal audit division of Banca del Gottardo where he was team leader and was promoted to Bank Officer in 1988 and then to Assistant Vice-President in 1989. In 1990, he was entrusted with several projects pertaining to organisation, and risk management control within the Financial and Risk Management Department. In 1996, he was promoted to Member of the Management and in 1999 became Head of Controlling at Group level. He joined BancaStato on 1 February 2003 as Head of the Financial and Risk Management Department, taking on de facto the position of Chief Financial Officer. On 1 April 2014, he became a member of the Executive Board and Head of Financial Services and Operations Division which is responsible for financial management and risk supervision, as well as for providing organisational, IT and operational support to various Bank processes.

### **Other activities**

- » Member of the Board of Directors of Tele Ticino SA, Melide;
- » Member of the Executive Committee and treasurer of the Swiss Walking Federation.

## **CLAUDIO GENASCI**

### **Function**

Member of the Executive Board since 1 January 2003; born on 26 February 1959, Swiss.

### **Education and professional background**

Degree in Economics and Social Sciences from the University of Fribourg in 1985. Hired at UBS SA as an all-rounder and later as an asset manager in their Finance Department in Lugano. Starting in 1990 he was Head of Asset Management at UBS SA in Locarno. He moved to Cornèr Banca SA, Lugano Offices, in 1996 as Head of Investment Strategies. He joined BancaStato on 1 August 2001 as Head of the Markets and Finances Division. In 2003, the Board of Directors appointed

him Member of the Executive Board for the Market and Finances Division. Since 16 April 2007 he has been Head of the Markets and Private Banking Division.

### **Other activities**

- » Member of the Board of Directors of Axion SWISS Bank SA, Lugano;
- » Chairman of the Foundation Council of the Fondazione di Previdenza Risparmio 3 of Banca dello Stato del Cantone Ticino;
- » Member of the Investment Committee of the Real Estate Fund Residentia, as an expert in real estate financing;
- » Member of the Board of Directors of SOAVE Asset Management Ltd., Lugano.

## **PATRICK LAFRANCHI**

### **Function**

Member of the Executive Board since 1 July 2017. Born on 22 October 1969, Swiss.

### **Education and professional background**

After graduating from the University of Zurich in 1996, and obtaining his lawyer's license, he joined BancaStato in 1998 as Head of Legal Affairs. In 2005, he was promoted to Member of Management and became Head of Credit Recovery. In 2012, he became Head of the Management and Credit Control Department. On 15 March 2017, he was appointed by the Board of Directors as a member of the Executive Board and Head of the Credit Management and Support Division.

## **GABRIELE ZANZI**

### **Function**

Member of the Executive Board as of 1 December 2017. Born on 22 August 1963, Swiss.

### **Education and professional background**

Degree in Economics from the University of Zurich in 1989. The next year he began his professional career at the Ticino Chamber of Commerce. In 1995 he joined UBS Ticino, assuming various positions with responsibility for Corporate clients. In 1998 he was employed by Credit Suisse, undertaking increasingly important functions. He was appointed

Head of Corporate Clients in 2012 and Regional Head for Ticino in 2016. Since 1 December 2017, he was the Head of Retail and Corporate at BancaStato.

### **Other activities**

- » Member of the Executive Committee of "Associazione Industrie Ticinesi AITI", Lugano;
- » Member of the Board of Directors of Hockey Club Lugano SA, Lugano;
- » Member of the Foundation Committee of the "Fondazione per il perfezionamento commerciale", Lugano.

## **5. COMPENSATION, PARTICIPATIONS AND LOANS**

### **5.1 Content and method of determining the compensation and the participation programs**

The fixed and variable compensation of the Executive Board, as well as that of the Chief Internal Auditor and his Deputy fall within the responsibility of the Board of Directors. Present compensations of the Members of the Board of Directors are established on the basis of a Resolution of the State Council dated 7 December 2016, effective 1 January 2017.

The Board of Directors approves the Staff Rules and Regulations and the Management Rules and Regulations. On an annual basis and acting on proposals from the Executive Board, the Board of Directors makes decisions with regard to the review of annual salaries and the variable component within the framework of MbO (management by objectives).

The social security coverage of the members of the Executive Board is calculated using the same parameters as used for calculating the compensation to all Members of the Management.

Guaranteed coverage exceeds minimum legal requirements. Moreover, they benefit from the family allowances granted to all staff.

The following figures include fixed retribution, variable retribution and a lump sum figure for entertainment expenses.

In 2017, total compensation for members of the Bank's bodies was as follows: CHF 508,086 for the Board of Directors and CHF 3,245,622 for the five members of the Executive Board. The highest compensation within the Board of Directors was

CHF 72,197 and the highest compensation within the Executive Board was CHF 794,360<sup>14</sup>.

Among the Bank's providers there are entities connected to the members of the Board of Directors and the Executive Board. The members of the Board of Directors and the members of the Executive Board benefit from mortgage loans under the same conditions as the Bank staff. At the end of 2017, loans to Bank governing bodies totalled CHF 109.7 million (see also the corresponding table of the Notes to the Financial Statements).

### **5.2 Transparency of the compensations, shareholdings and loans pertaining to issuers domiciled abroad**

As the Bank has no registered offices abroad, there is no relevant information under this point.

## **6. SHAREHOLDERS' PARTICIPATION RIGHTS**

### **Relations with Ownership**

The information to be disclosed as per paragraphs 6.1 to 6.5 of the Annex to the Directive on Information Relating to Corporate Governance issued by SIX Swiss Exchange does not apply to Banca dello Stato del Cantone Ticino. However, it was deemed useful to sum up the main features of the Bank's relation with its ownership. The members of the Board of Directors are appointed by the State Council. As laid down in Art. 33 of the Law on Banca dello Stato del Cantone Ticino, the Grand Council and the State Council ensure that the Law is adhered to and that the general policy of the Bank is in line with the objectives laid down in the Law. Within the authority of the Grand Council and the State Council lie, in particular, the overview and approval of the Bank's income statement and balance sheet.

In accordance with Art. 39 of the Law on Banca dello Stato del Cantone Ticino, the Board of Directors must submit its report on the state of business at the Bank, the income statement and the balance sheet, the proposal for appropriation of available earnings and the report of the External Auditors to the State Council by 31 March of every year.

By 30 April, the State Council transmits the documentation to the Grand Council for approval of the annual accounts, the proposed appropriation of available earnings and the sign off

<sup>14</sup> The Corporate Governance guidelines (which BancaStato implements on a voluntary basis) introduce more specific recommendations for the presentation of compensations within the Board of Directors and the Executive Board. We believe that the description contained in this Annual Report reflects the requirements for exhaustiveness and transparency.

of the Bank's governing bodies. In conformity with Art. 34 of the Law on Banca dello Stato del Cantone Ticino, the Grand Council exercises a supervisory duty as regards the fulfilment of the public mandate by way of the Public Mandate Control Commission. This Commission is made up of one member per parliamentary group each of whom is appointed by the Grand Council for a period corresponding to one legislative session.

In compliance with the provisions of Art. 35 of the Law on Banca dello Stato del Cantone Ticino, the Public Mandate Control Commission verifies the correct fulfilment of the public mandate and draws up a special report to the attention of the Management and Finance Commission on the achievement of the public mandate.

The report prepared by the Commission must include its opinion on the degree of fulfilment of the general and specific objectives laid down in the strategic document on the public mandate as drawn up by the Board of Directors and based in particular on its analysis of the Annual Social and Environmental Report.

The Commission, which details the parliamentary debate on the aforementioned documents with its report, is entitled to view all the documentation and to hear the Bank representatives insofar as this is compatible with banking secrecy.

**As of 31 December 2017, the Commission included:**

Nicola Brivio (Chairman as of June 2017), Pelin Kandemir Bordoli (Deputy Chairman as of June 2017), Maurizio Agustoni, Omar Balli (Chairman until June 2017), Claudia Crivelli Barella (took over from Michela Delcò Petralli in November 2017) and Gabriele Pinoja.

## **7. CONTROL AND DEFENCE MEASURES**

The information to be disclosed as per paragraphs 7.1 and 7.2 of the Annex to the Directive on Information Relating to Corporate Governance issued by SIX Swiss Exchange is not applicable to Banca dello Stato del Cantone Ticino.

## **8. AUDITORS**

### **8.1 Duration of the mandate and term of office of the Lead Auditor**

The appointment of the Auditors falls under the authority of the Board of Directors (Art. 37 of the Law on Banca dello Stato

del Cantone Ticino). In 2005, the Board of Directors entrusted the External Auditor mandate to PricewaterhouseCoopers SA in accordance with the Banking Law. In 2017, Ms. Glenda Brändli, partner at PricewaterhouseCoopers SA, assumed the function of Lead Auditor for the first time. This mandate was reassigned as the former Lead Auditor, Mr. Caloja, had performed this function for seven years, the maximum period set by the regulations. This mandate is annual.

PricewaterhouseCoopers SA also audits Axion SWISS Bank SA.

### **8.2 Auditing honorarium**

For the year 2017, the auditing honorarium of PricewaterhouseCoopers SA for the ordinary audit of BancaStato and other audits amounted to CHF 456,000.

### **8.3 Additional honorariums**

Other services from PricewaterhouseCoopers totalling CHF 20,000 were booked by BancaStato in 2017.

### **8.4 Supervisory and control instruments vis-à-vis the auditors**

As stated in the Section on the Board of Directors, the Audit and Risk Committee of the Board of Directors exercises various activities connected to the External Auditors.

The reports of the External Auditors are brought to the attention of the Board of Directors.

The Board of Directors meets at least once a year with the External Auditors. The full report of the External Auditors (including Group audits) on the financial statements as well as the report on the basic audit are presented by the External Auditors to the Board of Directors.

Representatives of the External Auditors take part in the meetings of the Audit and Risk Committee of the Board of Directors.

## **9. INFORMATION POLICY**

BancaStato's information and communication policy is based upon principles of consistency, clarity, continuity, up-to-datedness, transparency and verifiability. It specifically aims

to strengthen corporate culture and promote its image in observance of its corporate identity both within and without.

The responsibility for the management of the Bank's communication policy is entrusted to the Strategic Planning and Communications Department. The Bank has an Intranet site in which it informs all staff on corporate strategy, the products and services of the various divisions, financial results, press releases, as well as on communications from the Executive Board and the Board of Directors. This intranet website is an essential source of corporate information, truly a valuable resource comprising all documentation and data to facilitate the ongoing pursuit of banking activities.

Financial results are published twice a year and communicated to the Ticinese media (radio, television and newspapers as well as on the internet), to press agencies, as well as to the press offices of all Cantonal Banks and the Association of Swiss Cantonal Banks. As a rule, the annual financial report is presented during the first quarter at a press conference held at BancaStato's Head Office. The annual report is sent to the FINMA, the State Council, the Grand Council, the Public Mandate Control Commission, the Swiss National Bank, all Cantonal Banks, the Association of Swiss Cantonal Banks, as well as to correspondent banks, and Swiss and foreign clients upon request. Annual reports, in Italian and in English, can be accessed via the BancaStato website at [www.bancastato.ch](http://www.bancastato.ch)<sup>15</sup> and are available at any BancaStato counter.

For the 2017 financial year, the Bank published once again its Social and Environmental Report<sup>16</sup>. BancaStato can be accessed by the public via their website [www.bancastato.ch](http://www.bancastato.ch) which facilitate access to information on products, services and news from the Bank. The website [www.bancastato.ch](http://www.bancastato.ch) was developed in cooperation with IT professionals, it is updated on an ongoing basis and has become an interesting communication channel with the public.

The Bank publishes the magazine "BancaStato News"<sup>17</sup> and is present in various daily newspapers, broadcasts and publications which deal with financial and economic issues with interviews, presentations and financial articles<sup>18</sup>. These articles also appear on the website and, whenever possible, on the Bank's other communication channels in order to provide information on the diversified world of the Institution. BancaStato also posts its institutional news on Twitter.

Moreover, representatives from BancaStato participate regularly in conferences and other public events and respond to queries from the media with regard to the Bank's stance on topical issues.

The Executive Board receives journalists on a regular basis for the presentation of the financial reports and in order to introduce various issues relating to the Bank's activities, thus promoting dialogue and reciprocal knowledge.

All principal documents published by BancaStato are available at its branches and agencies as well as on its website. For further information, contact:

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<sup>15</sup> <http://www.bancastato.ch/bancastato/Area-media/Pubblicazioni/Rapporti-di-esercizio.html>

<sup>16</sup> <http://www.bancastato.ch/bancastato/Area-media/Pubblicazioni/Rapporti-di-esercizio.html>

<sup>17</sup> <http://www.bancastato.ch/bancastato/Area-media/Pubblicazioni/BancaStato-News.html>

<sup>18</sup> <http://www.bancastato.ch/bancastato/Area-media/Novita/Rassegna-stampa.html>

# Ticino's Economy in 2017 and Outlook for 2018

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## The international overview

While in 2016 major political and economic changes were unfolding in America, 2017 saw several elections in Europe that captured international attention. In March, the general elections in the Netherlands resulted in the victory of the Popular Party for Freedom and Democracy. Two months later, in France, Emmanuel Macron defeated the National Front candidate Marine Le Pen, averting the rise of the Le Pen movement and preserving the stability of the European project. Macron's poll results were reconfirmed by the legislative elections that guaranteed him a solid majority. In June, Theresa May called the voters to the polls in an attempt to achieve a stronger government in view of the Brexit negotiations with the European Community. However, the opposite resulted, compelling her to settle for a minority government. In September, the German CDU/CSU and SPD were confirmed as the principal parties in the Bundestag, albeit with a significantly lower percentage than in the 2013 elections. The Eurosceptic and highly nationalistic AfD entered into Parliament, having obtained 12% of the votes, obligating Chancellor Merkel to form a coalition government with the SPD. In October, elections were held in Austria to renew the Nationalrat and the Bundesrat, leading to the victory of the Austrian Popular Party with the Kurz list, characterised by highly nationalistic and conservative ideas. That same month, a referendum on the independence of Catalonia took place, causing an institutional conflict which opened a critical phase in the relations between the government and the regional Catalan police and the respective Spanish national institutions. The Catalan President remains abroad to avoid arrest by the Spanish authorities. Europe was also affected this year by a number of Islamist attacks while the war in Syria and Iraq is edging towards a conclusion as the territories occupied by ISIS are being retaken. With the completion of the most critical phase of the conflict, the tensions between the Kurdish people claiming their own territorial autonomy and Turkey have escalated. The latter approved a disputed institutional reform that concentrated legislative and judiciary powers in the hands of President Erdogan, causing concern throughout the international community. However, improvements in the

world geopolitical situation compared to 2016, as well as the results of the European elections, have kept the political risk of a strengthening of Eurosceptical movements at bay. This has also allowed accelerated global growth as compared to the previous year. According to the IMF, in 2017, the European and Asian areas recorded a greater positive variation than expected, growing by +2.2% and +5.4% respectively. Global growth was +3.7%, +0.5 percentage points above its 2016 level. The forecast for 2018 sets world growth at +3.9%. This estimate was reviewed upwards following the announcement of proposed tax cuts in the United States.

## The national overview

In 2017, Switzerland experienced minor GDP growth compared to 2016. According to SECO, 2017 is expected to close with an increase of +1%, 0.4 percentage points below the growth level recorded in the previous year. A +1.2% growth in household consumption and a +1.3% growth in State expenses are expected for 2017.

Investments in construction, and in machinery and equipment, are anticipated to grow by +1.2% and +2.8% respectively. The trade balance also continued to guarantee a positive contribution to the GDP (equivalent to approximately CHF 34.8 billion) with exports and imports increasing by +3.4% and +2.6% respectively, according to SECO estimates. In this context, occupation in terms of full time equivalents is believed to have increased by +0.4% in 2017 with a total number of employed exceeding 5 million in the third quarter of 2017. The growth in employment was diversified over the national territory: Zurich, the Mittelland and the North-West saw lesser growth than at the national level, while Central Switzerland and Ticino showed major growth. Still during the third quarter, unemployment according to the ILO was about 5%, below the 7.3% rate in the EU. Also in this case some regional differences can be pointed out, such as a higher unemployment rate in Ticino (5.4%) and in the Lemman region (7.9%). Unemployment calculated by SECO was approximately 3.2% in 2017, with minor cantonal differences compared to the preceding years.

The year 2017 also experienced a comeback of a certain level of inflation, estimated at +0.5% compared to the previous year, which has also affected import and export prices. With reference to the political situation, 2017 again saw some friction with the European Union over the implementation of the initiative against mass immigration, access to the EU financial markets by Swiss operators and the equivalence of the Swiss Stock Exchange. As regards referendums, the new energy reform (Energy 2050) was approved. This will lead to a gradual transfer of production towards renewable energy sources and to the progressive abandoning of nuclear power. Measures intended to address the Pension Reform (Previdenza 2020) and the Reform of Corporate Tax were rejected.

For 2018, SECO forecast a GDP growth of +2.3%, an increase compared to 2017. Household consumption is expected to grow by +1.4%, and public consumption by +0.7%. Investments in construction and equipment are anticipated to increase by +1.1% and +3.7% respectively, while the trade balance will contribute to a stronger GDP with exports and imports up by +4.5% and +3.9% respectively. In this context of growth, employment in fulltime equivalents is expected to further improve on an annual basis (+1.2%), with a SECO unemployment rate down to 2.9%. Consumer prices should remain stable at +0.3%.

### **The overview for Canton Ticino**

Based on BAK Basel data, Canton Ticino's real GDP grew by +1.4% in 2017. According to the last available update, GDP growth in Ticino is equivalent to what was experienced in 2016. The weakened Swiss franc with respect to the euro relieved some of the negative pressure on prices charged by some exporters, while other sectors continued to experience problems connected to a structural component. The business sector saw a further reduction of margins and sales which also affected employment, reducing the demand for labour. Compared to 2016, the banking sector saw an increase in profit and turnover. The digitization process brought about a structural transformation in this sector, reducing the need for labour while maintaining production output. The tourism branch

performed better than expected, with increased overnight stays and sales. As for the construction sector, its performance was stagnant at levels comparable to those of 2016. Still in 2017, the number of companies in the Commercial Registry increased, and positive results were also seen on the labour market. Unemployment, as measured by ILO standards, dropped to 5.4% during the third quarter of 2017, compared to 7.3% in the same quarter of the preceding year, while average SECO unemployment over the whole of 2017 was at 3.4%, down by 0.1 percentage point compared to the previous year. For 2018, BAK Basel anticipates a potential real GDP growth of 2.2%, equivalent to the national forecast.

# Report of the Board of Directors of Banca dello Stato del Cantone Ticino

## **Banca dello Stato del Cantone Ticino and the Economy of Switzerland and Ticino in 2017**

In Switzerland, 2017 continued to be characterized by negative interest rates on banks' deposits with the Swiss National Bank (SNB). These rates, which were introduced in January 2015 to counterbalance the strong Swiss franc, continued to impact negatively on banks' commercial margins on intermediate interest operations. In spite of the fact that the Swiss franc gradually weakened relative to the euro, therefore alleviating the negative pressure on Swiss exports, the SNB maintained its expansive monetary policy aiming at supporting the economy. The Swiss gross domestic product (GDP) experienced growth, although in a lesser degree than in 2016. The good performance of both the national and international economies and the absence of any particular destabilizing factors favoured the principal world stock exchanges, impacting positively on client asset volumes and financial transactions. Result from bank commission and trading business were favourably affected. In Ticino, the real estate sector which for several years has been under observation by economic operators, has continued to grow, but at a slower pace, while at the same time showing signs of saturation with a growing percentage of empty housing.

Looking more specifically at BancaStato's performance, 2017 brought again major satisfaction in terms of growing business volumes and results achieved in a market which may still objectively be termed difficult and characterized primarily by negative rates on short- and medium-term maturities. In the reporting year, the Bank successfully implemented its *light 2017* corporate strategy, aiming at streamlining operations, and, at the same time, it concluded the early retirement plan launched at the end of 2014. This plan is an essential step in attaining an optimum size without resorting to layoffs. This was all achieved effectively thanks to the progressive integration of the Group's operational processes with the Avaloq Source Master

IT platform adopted by BancaStato in April 2014 and by Axion SWISS Bank SA in January 2017.

The financial results achieved by BancaStato are in line with those produced in 2016. On the one hand, this has permitted an increase in the allocation to the Bank's owner from CHF 35.4 million to CHF 36.1 million and, on the other, it has bolstered the Bank's financial base through a substantial increase in its capital. Added to this is the interest on the subordinate loans of CHF 60 million and CHF 80 million granted by the Canton<sup>19</sup> at the end of 2014 and 2015 respectively, which brings the total payment to the Canton to CHF 40.2 million.

Client business volumes have continued to increase in both lending (+6.3% to CHF 10.4 billion) and funding (+6% to CHF 8 billion), which again confirms BancaStato's significant role in the economy of Ticino and its impact on its people.

The Bank's operating result increased by CHF 3 million, up from CHF 69 million to CHF 72 million (+4.4%). Net revenues showed a gratifying progression, totalling CHF 181.5 million, up by 1.9% compared to 2016. This growth refers to almost all sources of revenues with the exception of interest-earning transactions which were burdened by a major need for provisions in 2017 compared to 2016. On the back of an increase in operating expenses (+4.7% to CHF 101.9 million), due to a number of non-recurring elements, there was a considerable decrease in depreciation of fixed assets (-33.5% to CHF 7.6 million). Considering these excellent results, BancaStato made another important allocation of CHF 26 million to the reserves for general banking risks which, together with another CHF 12 million to the statutory retained earnings reserve, will further bolster the Institute's capital base. In spite of these substantial allocations, profit increased by CHF 1 million (+2%), to over CHF 48.1 million.

<sup>19</sup> For information about this loan, refer to Section 2.7 of the Corporate Governance chapter in this Annual Report.

### **Comment on the Evolution of Major Balance Sheet and Off-balance Sheet Items<sup>20</sup>**

Although BancaStato's business extends to all services typically offered by a universal bank, it continued to maintain its focus on mortgage lending in 2017. Mortgage loans increased by 7.4%, or CHF 605 million, exceeding CHF 8.8 billion. As interest rates remain at a historic low, the loan portfolio continues to be almost integrally structured on fixed rate mortgages. In this regard, and in consideration of concerns voiced over the past several years regarding a possible real estate bubble, it must be stated that BancaStato's lending policy continues to reflect a cautious approach. As a result, the quality of its lending portfolio has further improved. An analysis of mortgage loans shows that over 94% are first mortgages and almost 75% are for housing. The average mortgage granted for a single housing unit has slightly increased, but still remains around CHF 500,000, confirming the Bank a valuable resource for those Ticinese people wishing to buy their own home.

Amounts due from customers increased marginally (+CHF 11.1 million or 0.7%) just shy of CHF 1.6 billion. Loans to public corporations remained at their 2016 levels, totalling CHF 675 million, a threshold guaranteeing BancaStato's ability to maintain its dominant position in Ticino as regards this market segment. Loans to private individuals and companies were slightly up (+10.1 million or +1.1%) and reached CHF 920 million. These items are tangible signs of BancaStato's significant contribution to the development of the economy in the Canton.

As regards funding, payables resulting from client deposits once again showed a marked progression, up by CHF 454 million to almost CHF 8 billion. This 6% growth confirms the development which has been in progress for several years. Within this item, clients have turned primarily to savings accounts, which progressed by CHF 212 million and, in a smaller way, towards transactional accounts, which were up by CHF 165 million. Negative market rates, initially for all

durations up to 10 years and, during the second half-year, also for shorter terms, have once again caused a further major regression in all fixed term deposit items on the balance sheet (fixed savings and cash bonds).

In order to satisfy its requirements for medium to long-term funding, as well as to ensure sound management of exposure to interest rate risk, the Bank operated on the capital market<sup>21</sup> to substitute a CHF 200 million mortgage bond at 3% maturing in June 2017 with a new bond issue of the same value maturing in 2027 at 0.30%. Moreover, as it had done in previous years, it turned to bond issues of the Central Mortgage Bond Issuing Body of the Swiss Cantonal Banks (a net increase of CHF 74 million). This source provided medium- to long-term capital at a particularly low cost. Funding obtained on the capital market totalled CHF 2.6 billion at the end of 2017, representing a 2.9% increase.

The Bank's balance sheet total grew from close to CHF 12.2 billion at the end of 2016 to over CHF 12.6 billion as at 31.12.2017, exhibiting a further 3.6% progression. Looking back, the significant acceleration in the Bank's business volumes becomes even more noticeable. In fact, whereas in the ten-year period from 1991 to 2001 business volumes increased from CHF 4.3 billion to CHF 6.3 billion (an approximate 50% growth), they have doubled over the past 15 years.

With respect to off-balance sheet operations, as regards contingent liabilities, guarantees provided by the Bank were just shy of CHF 97 million on 31.12.2017, on the same level as in the previous year. However, commitments arising from documentary letters of credit connected to Commodity & Trade Finance, saw a slight CHF 15 million regression, down to CHF 37 million. Irrevocable commitments decreased by approximately CHF 20 million in the context of new mortgage loans to be granted at a later date.

<sup>20</sup> The data refer to BancaStato's Individual financial statements. A distinction is made between Individual and Group statements only in the case of significant variances.

<sup>21</sup> The 0.30% bond issue of Banca dello Stato del Cantone Ticino 2017-2027 was floated with the support of BNP Paribas and Credit Suisse.



### **Evolution of Assets under Management**

Assets under management at the BancaStato Group exhibited a clear progression during 2017, up from CHF 14.3 billion at the end of 2016, to CHF 15.6 billion at 31.12.2017, a 9.3% growth.

The volume of assets under management at BancaStato increased by CHF 926 million (+ 9%), levelling close to CHF 11.3 billion. In 2017, inflow in net new money, CHF 559 million, was once again particularly gratifying, as was the evolution of assets resulting from the good performance in stock and forex markets which yielded a positive CHF 367 million performance. By the end of 2017, assets under custody totalled CHF 614 million, down from CHF 878 in 2016.

Assets under management by Axion SWISS Bank SA also clearly showed a positive evolution, growing by CHF 406 million to almost CHF 4.4 billion (+10.2%). The inflow of net new money amounted to CHF 87.3 million, a positive performance just under CHF 319 million.

### **Comment on the Evolution of the Main Items of the Income Statement**

In 2017 BancaStato was able to consolidate the outstanding results achieved in the preceding year, reconfirming its position as a valuable source of income for the Canton's treasury. The operating result for 2017, CHF 72 million, exceeded by a substantial CHF 3 million the already remarkable result achieved by the Bank in the previous year. BancaStato again seized this opportunity to bolster its capital with an allocation of CHF 26.1 million to Reserves for general banking risks (CHF 22 million in 2015 and CHF 24 million in 2016).

In spite of this major allocation, net income and, consequently, also the payment to the Canton was up by 1.8% from CHF 35.4 million for 2016 to CHF 36.1 million for 2017.

Considering the interest paid out to the Canton on the subordinated loans granted to the Bank, the total payment was up from CHF 35 million in 2015 to CHF 39.5 million in 2016, and CHF 40.2 million for the 2017 financial year.

Net revenues for 2017 totalled CHF 181.5 million, up by 1.9% or CHF 3.3 million.



The gross results from interest activities, traditionally the principal revenue item for BancaStato, continued its progressive trend of the previous years, and grew by over CHF 2 million (or +1.5%). This evolution was supported on the one hand by an increase in mortgage volumes in recent years as well as by commercial margins and, on the other, by opportunities being offered in the current market environment for low-cost financing. As a result of continuing negative market rates on short and medium-term operations, the trend of shrinking margins on client deposits continues. In this context, BancaStato achieved gratifying results by maintaining its cautious policy with respect to the management of its balance sheet structure, as well as by turning to issues of the Cantonal Banks' mortgage refinancing institute in order to adequately refinance existing outstanding loans. Net result from interest operations (CHF 129.1 million or -2.3%) was however affected by an increased need for provisions for lending activities.

The results from commission business and services progressed substantially by CHF 2.6 million, just below 10%, levelling at CHF 29.1 million. This was due primarily to commission income from securities trading and investment activities (+ CHF 2.1

million) which have benefited from the increase in assets under management and the positive trend in financial markets. Other components of Result from commission business (lending operations and service fee activities) also contributed to the global development of commission income.

Trading income performed as well, showing a 10.7% progression equivalent to CHF 1.4 million, and reaching CHF 14.7 million. This result is due to increased operational demand on the part of clients as well as to improved trading results on the part of the Institute.

Other results from ordinary activities again improved by over 30%, from CHF 6.3 million in 2016 to CHF 8.7 million in 2017 (+36.7%). Among the major contributing factors were the sale of a security in the financial investments portfolio (+CHF 1 million), the increased dividends from the direct subsidiaries of the BancaStato Group (+CHF 0.7 million) and from the management of the Bank's buildings (+CHF 0.7 million).

Operating expenses were up by 4.7%, from CHF 97.3 million in 2016 to CHF 101.9 million in 2017. Personnel expenses increased by CHF 3.6 million and reached CHF 68.5 million.

This is also due to non-recurring factors connected to staff pension fund. Other operating expenses were affected primarily by increased regulatory requirements which impact on costs connected to IT programmes and the provision of technical-financial information for their functioning.

Value adjustments on participations and depreciation and amortisation of tangible fixed assets and intangible assets, regressed by CHF 3.9 million (-33.5%), down to CHF 7.6 million primarily as a result of decreased costs in relation to the depreciation of the informatics platform.

The item "Changes to provisions and other value adjustments, and losses"<sup>22</sup> recorded in 2017 a release of CHF 80,000 against a net requirement of CHF 0.4 million in the preceding year.

Operating results for 2017 exceeded CHF 72 million with a gratifying growth of CHF 3 million (+4.4%), setting a new record over the previous year.

The item "Extraordinary income" remained stable at the same levels as the previous year and was almost entirely the result of the payment extended over several years of a participation of BancaStato in the capital of Swisscanto Holding AG (assigned to Zurich Cantonal Bank in 2015).

In consideration of the excellent ordinary and extraordinary income achieved, the Board of Directors chose to further bolster the Bank's capital and financial base by allocating CHF 26.1 million to the Reserve for general banking risks, CHF 2.1 million more than in the preceding year.

This major allocation did not affect the growth in net income, which progressed by 2%, up from CHF 47.2 million in 2016 to CHF 48.1 million in 2017. As has already been mentioned, this growth is to the advantage of the Bank's owner as the payment to the Canton was augmented from CHF 35.4 million in 2016 to CHF 36.1 in 2017 (+1.8%). Adding to this payment is the interest on the subordinated loans of CHF 60 million (since end-2014) and CHF 80 million (since end-2015) granted by the Canton to BancaStato. This interest represents a further CHF 4.1 million being injected into the State coffers in 2017. Overall, BancaStato paid out to the Canton CHF 40.2 million in 2017 compared to CHF 39.5 million in 2016.

This payment is a valuable source of income for the public body. An analysis of the evolution of this item over the last decade shows that the payment to the Canton has substantially

increased (+69.1%), from CHF 23.8 million in 2007 to CHF 40.2 million in 2017 (considering the overall payment). Still over the last decade, BancaStato paid out close to CHF 313 million. Considering that the endowment capital was increased from CHF 240 million to CHF 300 million as at 31.12.2017, it can be said that the Institute repaid over 100% of the Canton's initial investment.

As for the results of Axion SWISS Bank SA<sup>23</sup>, both net revenues and operating expenses increased substantially in all component items due to the acquisition of a share of client assets from SGPB Lugano which became effective at the beginning of March 2016. This was paired with the assimilation of part of their staff. Net income rose from CHF 26 million in 2016 to CHF 31.1 million in 2017 (+19.6%), while operating costs increased from CHF 19.9 million to CHF 22.7 million (+14.3%).

Among revenue items, results from interest operations grew from CHF 5.2 million in 2016 to CHF 8.6 million in 2017 (+64.9%) thanks to careful management of the balance sheet structure, especially with regards to balances in foreign currency on client current accounts. These were however penalized by negative market rates applied to short- and to medium-term both for CHF and EUR. The result from commission business and services, the principal source of revenue for a private-banking-oriented bank, saw further growth, up from CHF 16.9 million in 2016 to CHF 18.9 million in 2017 (+11.7%). This stemmed primarily from client asset management and securities operations. Income from trading activities, CHF 3.6 million, remained on the same excellent levels recorded in the previous year.

The increase in operating expenses, which includes both personnel (+5.9%) and other operating expenses (+37.9%), was due, as mentioned previously, to the operation which took place in the spring of 2016 and, as regards the second item, to the adoption of the common informatics platform with BancaStato.

The item Value adjustments on participations and depreciation and amortization of tangible fixed assets and intangible assets results – as in the preceding year – from the depreciation of goodwill following the 2016 operation.

In spite of all this, the operating results and net income evolved in a gratifying manner, progressing by 19% to CHF 3 million (+0.5 million) and 16.2% to CHF 2.3 million (+CHF 0.3 million) respectively. This allowed a major distribution to the Parent Bank.

At the consolidated level, the Group's profit remained at the same level as previous year, CHF 44.8 million (-0.5%).

<sup>22</sup> Since 2015, in accordance with FINMA Circular 2015/01 "Accounting – banks", this item shows only operating losses and changes to provisions for other banking risks.

<sup>23</sup> For further information on the results of Axion SWISS Bank SA, refer to its Annual Report.

## Profitability, Efficiency and Financial Strength

BancaStato's profitability in terms of Return on Equity (ROE)<sup>24</sup> remained at the excellent levels as in the previous year (8.3%), thus fulfilling the expectations of its owner (in this regard, it should be mentioned that in 2010 this indicator stood at 5.5%). Return on Risk Adjusted Capital (RORAC) further improved, up from 14.6% in 2016 to 14.9% in 2017.

The efficiency indicators, a ratio of operating expenses (whether they include depreciation and provisions for other operating risks or not) to income (Cost / Income I e II), the Bank consolidated the progressive positive trend it has demonstrated since 2010. Cost / Income I (which does not consider depreciation and provisions for other business risk incurred during the year) evolved from 54.6% in 2016 to 56.1% in 2017 (against a 67.3% indicator in 2010), while Cost / Income II (which considers all costs, depreciation and provisions during the year) further improved from 61.3% in 2016 to 60.3% in 2017 (76.4% in 2010). The strategic measures implemented by the Bank in the last decade got its profitability off the ground. The Institute's operating result doubled over 8 years (from CHF 35.2 million in 2010 to CHF 72 million in 2017).

Staff levels declined from 392.90 full time equivalents (FTEs) at 31 December 2016 to 388.05 FTEs at the end of 2017.

The Bank's capital adequacy, as determined by the ratio of required capital to available funds<sup>25</sup>, showed from end 2011 to the present, changes resulting from stricter requirements on the part of the surveillance authority, set against increases in endowment capital granted by the Canton and allocations to reserves decided by the Institute in the light of progressive excellent financial results achieved. Therefore, on the back of the coverage ratio of required capital with available (including the countercyclical buffer introduced by the Federal Council in 2013 and doubled in the following year) stood at 196% at the end of 2011, after fluctuating from a minimum of 178.1%

(31.12.2013) to a maximum of 211.9% (31.12.2015), this coverage ratio stood at 196.5% at the end of 2017 (16.5% solvency ratio, against a minimum FINMA requirement of 15.7% – including the countercyclical buffer). Let it be reminded that for BancaStato – which for its size and profile is included in category IV banks – the minimum regulatory requirement is 140% (equivalent to a solvency ratio of 11.2% and to a minimum FINMA requirement of 12%).

It must be noted that the indicator for Core Tier 1 – CET 1 capital has improved from 12.9% at the end of 2016 to 13.9% at 31.12.2017 while the Tier 1 capital indicator remained at the same levels as in the previous year (15.2%). Both indicators more than satisfy the minimum requirements.

This results, on the one hand, from the reimbursement of a subordinated loan of CHF 60 million with PONV clause (formerly included in Tier 1) granted to the Bank by the Canton in 2014 and from the increase of the same amount of the endowment capital at the end of 2017 (the CHF 300 million endowment capital is booked under Core Tier 1, which stands for better-quality capital) and, on the other hand, from the allocation to Reserves for general banking risks of CHF 26.1 million earmarked at the end of 2017 (compared to CHF 22 million in 2015 and CHF 24 million in 2016).

Capital adequacy at the consolidated level is marginally better compared to the individual financial statements, with a coverage ratio increasing from 199.3% at the end of 2014 to a maximum of 219.2% at 31.12.2015, decreasing to 216.4% at the end of 2016, and to 204.4 at 31.12.2017, taking into account the countercyclical capital buffer introduced by the Federal Council in order to restrain an overheated real estate market. The Group's indicators as set by the Bank for International Settlements evolved in a much similar manner as those of the Individual accounts, namely:

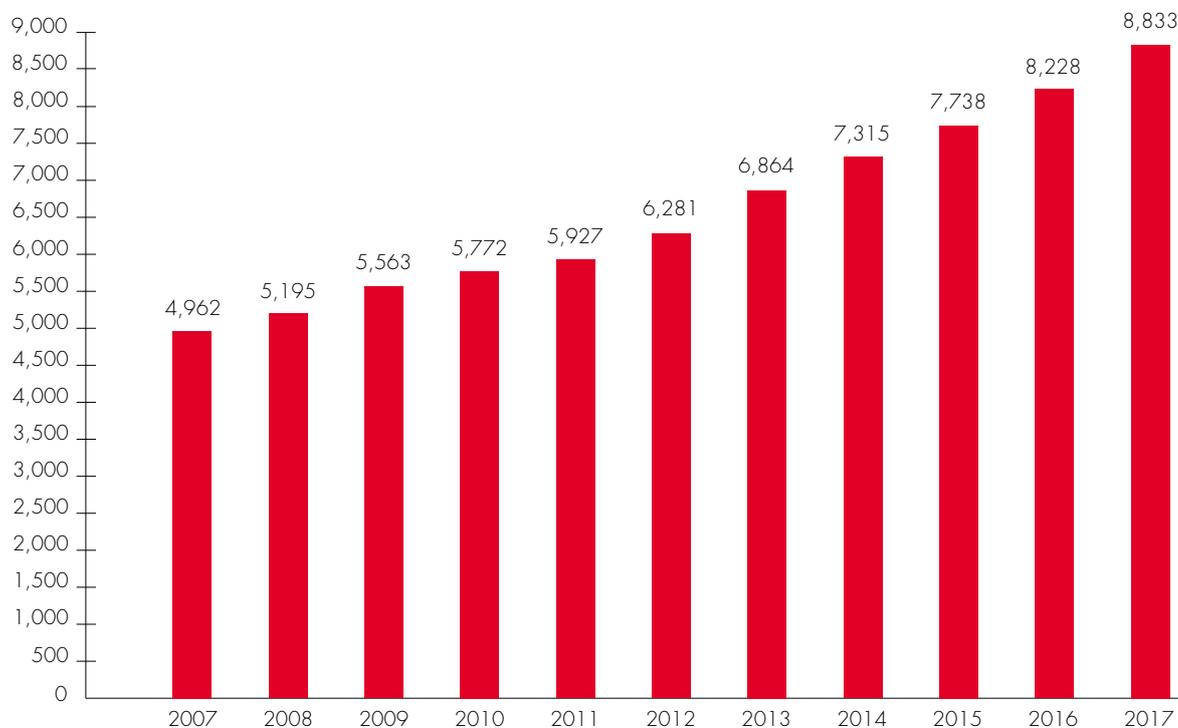
BIS adequacy indicators	Without countercyclical buffer		With countercyclical buffer	
	2017	2016	2017	2016
Core Tier 1 (CET1)	14.6%	13.5%	13.6%	12.8%
Tier 1 (T1)	15.8%	15.7%	14.9%	14.9%
Total regulatory capital	17.1%	17.3%	16.4%	16.6%

<sup>24</sup> The reference used to calculate ROE is net revenues before allocation to the reserve for general banking risks, while the reference capital comprises average core capital of the reporting year (net of any increase in endowment capital at year-end and of the year's allocation to reserves for general banking risks).

<sup>25</sup> Calculated on the basis of Basel III rules set by the Bank for International Settlements.

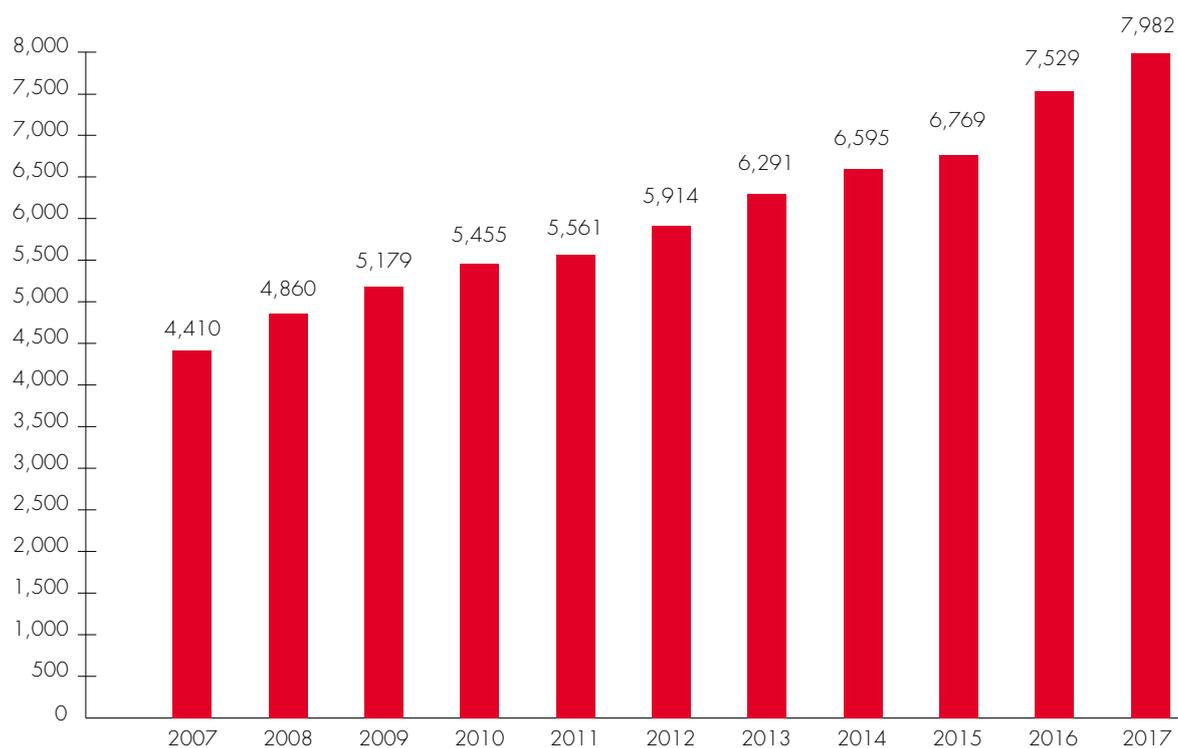
## EVOLUTION OF MORTGAGE LENDING

(CHF millions)



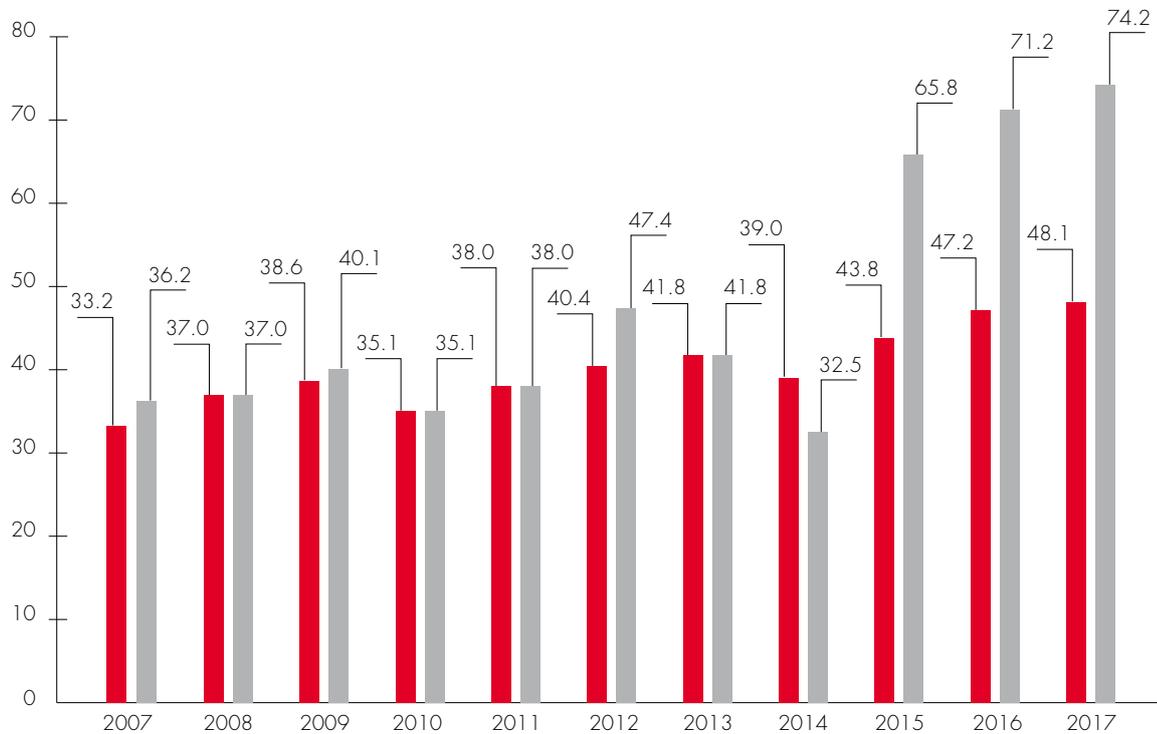
## EVOLUTION OF TOTAL AMOUNTS DUE TO CUSTOMERS

(CHF millions)



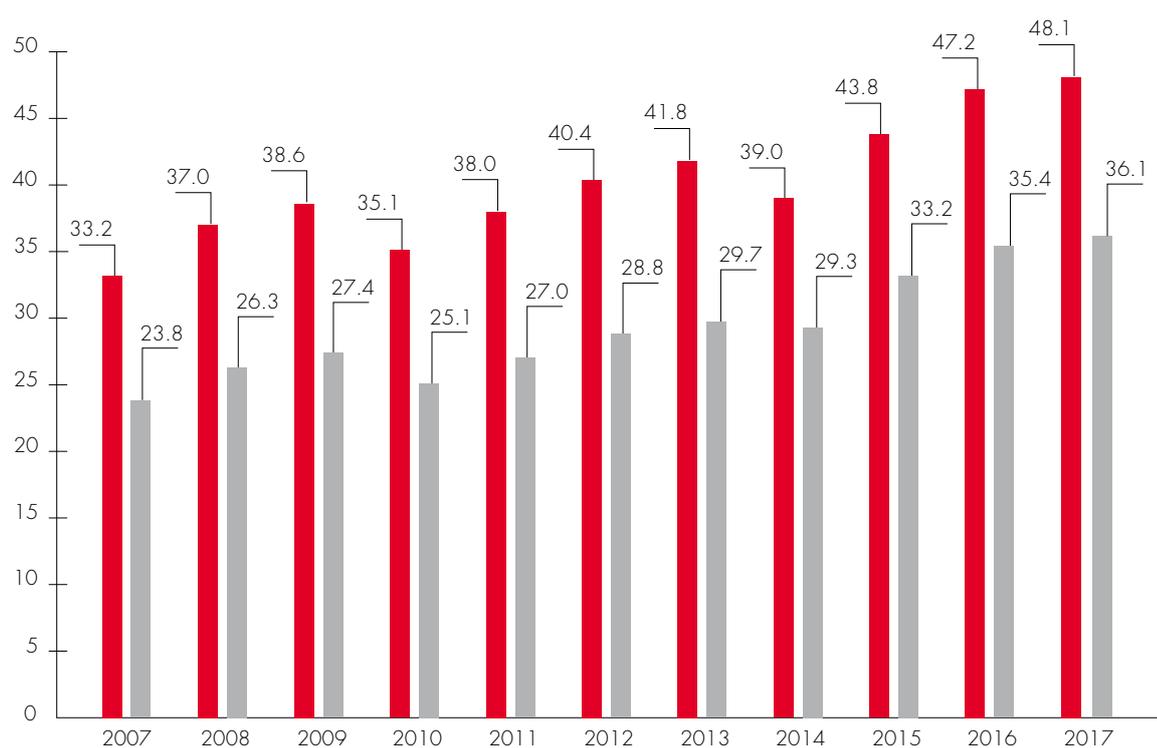
## EVOLUTION OF NET INCOME

(CHF millions) ■ Net income ■ Net income before the allocation to reserves for general banking risks



## EVOLUTION OF THE PAYMENT TO THE CANTON

(CHF millions) ■ Net income ■ Payment to the Canton





# Group Financial Statements

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# 1. Consolidated Balance Sheet

(CHF thousands)	Notes	31.12.2017	31.12.2016	Change
<b>Assets</b>				
Liquid assets		2,036,626	2,204,767	-168,141
Amounts due from banks		262,761	295,736	-32,975
Amounts due from customers	5.10.2	1,875,231	1,845,418	29,813
Mortgage loans	5.10.2	8,832,812	8,227,790	605,022
Trading portfolio assets	5.10.3	40,833	27,793	13,040
Positive replacement values of derivative financial instruments	5.10.4	51,607	24,069	27,538
Financial investments	5.10.5	295,413	295,498	-85
Accrued income and prepaid expenses		12,002	13,450	-1,448
Non-consolidated participations	5.10.6 and 5.10.7	6,529	6,389	140
Tangible fixed assets	5.10.8	80,111	82,400	-2,289
Intangible assets	5.10.9	14,302	21,364	-7,062
Other assets	5.10.10	17,774	278,673	-260,899
<b>Total assets</b>		<b>13,526,001</b>	<b>13,323,347</b>	<b>202,654</b>
Total subordinated claims		20,419	22,454	-2,035
<i>of which subject to mandatory conversion and/or debt waiver</i>		20,419	21,985	-1,566
<b>Liabilities</b>				
Amounts due to banks		517,529	856,284	-338,755
Liabilities from securities financing transactions	5.10.1	70,000	125,000	-55,000
Amounts due in respect of customer deposits		9,102,551	8,762,224	340,327
Negative replacement values of derivative financial instruments	5.10.4	28,663	52,290	-23,627
Cash bonds		1,105	3,187	-2,082
Bond issues and central mortgage institution loans	5.10.11 and 5.10.13	2,617,000	2,543,000	74,000
Accrued expenses and deferred income		42,012	43,078	-1,066
Other liabilities	5.10.10	125,935	11,783	114,152
Provisions	5.10.14	3,600	4,225	-625
Reserves for general banking risks	4 and 5.10.14	438,000	411,886	26,114
Endowment capital	4	300,000	240,000	60,000
Statutory retained earnings reserve	4	234,772	225,324	9,448
Group profit	4	44,834	45,066	-232
<b>Total liabilities</b>		<b>13,526,001</b>	<b>13,323,347</b>	<b>202,654</b>
Total subordinated liabilities		255,273	315,273	-60,000
<i>of which subject to mandatory conversion and/or debt waiver</i>		80,000	140,000	-60,000
<b>Off-balance sheet transactions</b>				
Contingent liabilities	5.10.2 and 5.11.21	140,081	145,298	-5,217
Irrevocable commitments	5.10.2	49,613	63,536	-13,923
Obligations to pay up and make further contributions	5.10.2	14,180	14,180	-

## 2. Consolidated Income Statement

(CHF thousands)	Notes	2017	2016	Change
<b>Income and expenses from ordinary banking activities</b>				
<b>Result from interest operations</b>				
Interest and discount income		187,970	184,445	3,525
Interest and dividend income from trading portfolios		-	46	-46
Interest and dividend income from financial investments		2,790	3,608	-818
Interest expense		-45,798	-48,544	2,746
<b>Gross result from interest operations</b>		<b>144,962</b>	<b>139,555</b>	<b>5,407</b>
Changes in value adjustments for default risks and losses from interest operations		-7,300	-2,277	-5,023
<b>Net result from interest operations</b>		<b>137,662</b>	<b>137,278</b>	<b>384</b>
<b>Result from commission business and services</b>				
Commission income from securities trading and investment activities		47,331	42,511	4,820
Commission income from lending activities		3,783	3,333	450
Commission income from other services		10,358	9,982	376
Commission expense		-12,566	-11,407	-1,159
<b>Result from trading activities and fair value option</b>	5.12.23	<b>18,291</b>	<b>16,791</b>	<b>1,500</b>
<b>Other results from ordinary activities</b>				
Result from the disposal of financial investments		1,289	623	666
Income from participations		710	452	258
<i>of which from participations valued using the equity method</i>		40	65	-25
<i>of which non-consolidated participations</i>		670	387	283
Result from real estate		144	176	-32
Other ordinary income		1,740	2,037	-297
Other ordinary expenses		-168	-15	-153
<b>Net revenues</b>		<b>208,574</b>	<b>201,761</b>	<b>6,813</b>
<b>Operating expenses</b>				
Personnel expenses	5.12.25	-83,934	-79,416	-4,518
Other operating expenses	5.12.26	-38,771	-37,063	-1,708
<b>Value adjustments on participations and depreciation and amortisation of tangible fixed assets and intangible assets</b>	5.10.8 and 5.10.9	<b>-16,381</b>	<b>-17,390</b>	<b>1,009</b>
<b>Changes to provisions and other value adjustments, and losses</b>		<b>-50</b>	<b>-430</b>	<b>380</b>
<b>Operating result</b>		<b>69,438</b>	<b>67,462</b>	<b>1,976</b>
<b>Extraordinary income</b>	5.12.27.02	<b>2,553</b>	<b>2,518</b>	<b>35</b>
<b>Extraordinary expenses</b>	5.12.27.02	<b>-16</b>	<b>-42</b>	<b>26</b>
<b>Changes in reserves for general banking risks</b>	5.12.27.04	<b>-26,114</b>	<b>-24,000</b>	<b>-2,114</b>
<b>Taxes</b>	5.12.28	<b>-1,027</b>	<b>-872</b>	<b>-155</b>
<b>Group profit</b>		<b>44,834</b>	<b>45,066</b>	<b>-232</b>

### 3. Cash Flow Statement

(in CHF thousands)	2017		2016	
	Cash inflow	Cash outflow	Cash inflow	Cash outflow
<b>Cash flow from operating activities (internal financing)</b>	<b>426,694</b>	<b>-</b>	<b>12,295</b>	<b>-</b>
Group result	44,834	-	45,066	-
Change in reserves for general banking risks	26,114	-	24,000	-
Depreciation of fixed assets	16,381	-	17,390	-
Change in value adjustments for default risks and losses	-	625	-	1,177
Accrued income and prepaid expenses	1,448	-	3,617	-
Accrued expenses and deferred income	-	1,066	5,036	-
Other assets and liabilities	351,608	-	-	48,402
Interest on the endowment capital of the previous year	-	12,000	-	12,000
Previous financial year dividend	-	-	-	21,235
<b>Cash flow from endowment capital transactions</b>	<b>59,825</b>	<b>-</b>	<b>-</b>	<b>-</b>
Endowment capital	60,000	-	-	-
Change in scope of consolidation	-	175	-	-
<b>Cash flow from transactions in respect of participations, tangible fixed assets and intangible assets</b>	<b>-</b>	<b>7,170</b>	<b>-</b>	<b>40,367</b>
Non-consolidated participations	-	140	136	1,709
Real estate	-	2,139	-	11,519
Other tangible fixed assets	-	4,891	-	6,890
Intangible assets	-	-	6,298	26,683
<b>Cash flow from banking operations</b>	<b>-</b>	<b>647,490</b>	<b>940,176</b>	<b>-</b>
<b>Medium and long-term business (&gt;1 year)</b>	<b>-</b>	<b>622,586</b>	<b>-</b>	<b>661,754</b>
Amounts due in respect of customer deposits	-	82,109	-	70,167
Cash bonds	-	2,082	-	2,578
Bond issues and central mortgage institution loans	294,000	220,000	320,000	288,000
Bond issues	-	-	50,000	-
Amounts due from customers	-	7,458	-	152,991
Mortgage loans	-	605,022	-	489,386
Financial investments	85	-	-	28,632
<b>Short-term business</b>	<b>-</b>	<b>24,904</b>	<b>1,601,930</b>	<b>-</b>
Amounts due to banks	-	338,755	175,734	-
Liabilities from securities financing transactions	-	55,000	48,861	-
Negative replacement values of derivative financial instruments	-	23,627	10,831	-
Amounts due in respect of customer deposits	422,436	-	1,359,776	-
Trading portfolio	-	13,040	3,180	-
Positive replacement values of derivative financial instruments	-	27,538	23,125	-
Amounts due from banks	32,975	-	-	111,403
Amounts due from customers	-	22,355	91,826	-
<b>Liquidity</b>	<b>168,141</b>	<b>-</b>	<b>-</b>	<b>912,104</b>
Changes in liquidity	168,141	-	-	912,104
	<b>654,660</b>	<b>654,660</b>	<b>952,471</b>	<b>952,471</b>

## 4. Statement of Changes in Equity

(CHF thousands)	Paid out endowment capital	Retained earnings reserve	Reserve for general banking risks	Result of the period	Total
<b>Equity at 1.1.2017</b>	240,000	225,324	411,886	45,066	922,276
<b>Appropriation of retained earnings 2016</b>					
<i>Assignment to the retained earnings reserve</i>	-	+9,623	-	-9,623	-
<i>5% interest on the endowment capital</i>	-	-	-	-12,000	-12,000
<i>Additional payment to the Canton</i>	-	-	-	-23,443	-23,443
Endowment capital increase	60,000	-	-	-	60,000
Changes in the reserves for general banking risks	-	-	+26,114	-	26,114
Group profit	-	-	-	+44,834	44,834
AHSA Holding SA in liquidation <sup>1</sup>	-	-175	-	-	-175
<b>Total equity at 31.12.2017</b>	<b>300,000</b>	<b>234,772</b>	<b>438,000</b>	<b>44,834</b>	<b>1,017,606</b>

<sup>1</sup> The capital of AHSA Holding SA was reimbursed but the deletion from the Commercial Registry of Canton Ticino has not been completed.

## 5. Notes to the Financial Statements

### 5.1 GROUP ACTIVITIES AND PERSONNEL

#### 5.1.1 Group Activities

Banca dello Stato del Cantone Ticino, BancaStato, based in Bellinzona, is an autonomous banking institution under public law which operates as a full service bank whose primary aim is to favour the development of the economy in Ticino.

Its operations have evolved over 100 years and comprise the complete range of services provided by full service banks. These activities are geared towards facilitating access to capital for small and medium-sized companies as well as individuals.

In 2010 and 2013, as part of a move to diversify its sources of revenue, BancaStato acquired the entire capital of AHSA Holding SA, Lugano, in order to gain indirect control over Axion SWISS Bank SA, Lugano (Axion). At end-2016, BancaStato acquired the entire capital of Axion from AHSA Holding SA. During 2017 the capital of AHSA Holding SA was entirely reimbursed but the cancellation from the Commerce Registry of Canton Ticino is still pending.

Axion Swiss Bank SA's core business is asset management for private as well as institutional clients, and it is active in the principal directly related services, as securities and currency intermediation on the main international markets, investment advisory and lending. Operations in the lending business is prevalently limited to Lombard loans, i.e. in advances on deposited assets. During the first quarter of 2016, in the framework of a strategy aimed at strengthening its asset administration business, Axion acquired a portion of the infrastructure and client assets of Société Générale Private Banking (Lugano-Svizzera) SA.

With the aim of jointly creating a service platform for external asset managers, BancaStato acquired, in 2016, a minority share (30%) in Soave Asset Management Ltd., Lugano as well as a minority share (30%) in Londinium Dac, Dublin. Soave Asset Management Ltd. is active in asset management while Londinium Dac is a company authorized to operate as an investment company in accordance with the MiFID, providing onshore investment and savings management services.

##### 5.1.1.1 Balance sheet transactions

Interest-earning transactions are largely executed with customers and they represent the Group's primary source of revenue. Loans to customers are generally secured by mortgages, and most lending is used to finance housing properties. Commercial loans are either secured against collateral or are unsecured.

Interbank operations almost entirely consist of short-term transactions. In consideration of the current crisis in the

financial sector, interbank exposure has been reduced by giving preference to deposits at the Swiss National Bank. For medium and long-term funding, BancaStato turned to the capital market. In addition, it is a member of the Central Mortgage Bond Issuing Body of the Swiss Cantonal Banks and therefore regularly utilises bond issues floated by this institution.

The Banks of the Group hold a strategic security portfolio in medium to long-term investments, booked under financial investments.

##### 5.1.1.2 Trading operations

The Group performs, on behalf of its customers, the full array of foreign exchange trading services offered by banks. Moreover, it trades on its own account in foreign exchange as well as, to a limited extent, in debt securities (bonds), equity securities (shares and participation certificates), investment funds and metals.

Currency trading operations on foreign currencies on the Bank's own account are limited to a small number of currencies for which a liquid market exists.

##### 5.1.1.3 Commission business and services

Asset management and administration, payment transactions, as well as trading in securities and financial instruments on behalf of customers and loan related business, constitute the bulk of the Bank's commission activities and other services.

#### 5.1.2 Group personnel

As at 31 December 2017, the Group had a total of 486 employees on payroll, i.e. 446.15 full-time equivalents (FTEs) with apprentices calculated at 50%, compared to 504 employees at the end of 2016 (463.50 FTEs).

#### 5.1.3 Outsourcing

The Group outsources a number of its business services as defined by the FINMA Circular 2008/7 "Outsourcing - Banks". This includes payment transaction services, securities administration, the printing and sending out of banking documents and the management of IT systems (central informatics and work stations) which are performed by the service provider Avaloq Sourcing (Switzerland & Liechtenstein) SA, Bioggio.

In addition to the activities listed in the FINMA Circular, the Group contracts out activities pertaining to building management and maintenance as well as supplies. Within the Group, Axion outsources a number of services to BancaStato.

## 5.2 ACCOUNTING AND VALUATION PRINCIPLES

### 5.2.1 General principles

The accounting and valuation principles referred to by the Group and its various entities comply with the provisions of the Swiss Code of Obligations (CO), the Swiss Federal Law on Banks and Savings Banks (Banking Act), the Ordinance on Banks and Savings Banks (Banking Ordinance) and the guidelines issued by the Swiss Financial Market Supervisory Authority (FINMA), in particular the FINMA Circular 2015/1 "Accounting - banks".

The Group's financial statements are prepared on the basis of regular reporting and comply with the true and fair view principle.

All transactions are recorded at the time they are concluded. The balance sheet is presented on a transaction date basis.

### 5.2.2 General valuation principles

The financial statements are prepared on the going-concern assumption. The accounting is therefore based on going-concern values.

Assets are defined as laid down in Art. 959.2 CO. If a reliable estimate of an asset is not possible, this item is considered a contingent asset and is commented on in the Notes to the Financial Statements.

Liabilities are defined as laid down in Art. 959.5 CO. If a reliable estimate of a liability is not possible, this item is considered a contingent liability and is commented on in the Notes to the Financial Statements.

Balance sheet items and off-balance sheet items are valued individually. The Group does not apply the transitional provision of Art. 69.2 of the Banking Ordinance which allows the individual valuation of tangible fixed assets and intangible assets by 1 January 2020 at the latest.

In principle, neither assets and liabilities nor expenses and income are allowed to be offset.

Receivables and payables are offset only in the following cases:

- deduction of value adjustments from the corresponding asset item;
- own debt securities and similar instruments are offset with the corresponding items in the liabilities;
- offsetting of positive and negative changes in book value with no income effect in the current period in the compensation account.

### 5.2.3 Financial instruments

#### 5.2.3.1 Liquid assets

Liquid assets are recognized at their nominal value.

#### 5.2.3.2 Securities financing transactions

The item "Amounts due to and from securities financing transactions" comprises any receivables or payables from securities repurchase agreements effected with other banks through the Eurex REPO platform. The guarantees, which are part of the SNB basket, are revaluated on a daily basis, and any excess or shortage of coverage is settled directly through the clearing-house (SIX Group AG).

#### 5.2.3.3 Amounts due from banks, amounts due from customers and mortgage loans

These are entered at their nominal value. Receivables are evaluated individually according to uniform standards established to analyse the borrowers' solvency and the value of the collateral provided. For non-performing and impaired loans, value depreciation is covered by individual value adjustments which are directly offset by assets, with collateral considered at its liquidation value.

Value adjustments for risk of default that are no longer economically necessary, and are not used for other similar requirements, are released through the income statement via the item "Changes in value adjustments for default risk and losses from interest operations".

Precious metal account deposits are valued at fair value provided the precious metal concerned is traded on a price-efficient, liquid market.

#### 5.2.3.4 Amounts due to banks and amounts due in respect of customer deposits

These items are recognised at their nominal value.

Amounts due in respect of precious metal account deposits are valued at fair value if the precious metal concerned is traded on a price-efficient, liquid market.

#### 5.2.3.5 Trading activities and trading portfolio liabilities

The valuation of the portfolio of securities and metals held for trading purposes is at fair value. If, in exceptional cases, fair value cannot be determined, the valuation and recognition will be based on the lower of cost or market principle.

Gains and losses, as well as adjustments to the above-mentioned rate changes and the revenue from interest and dividends, are booked under "Result from trading operations and fair value option".

### 5.2.3.6 Positive and negative replacement values of derivative financial instruments

Derivative financial instruments include options, futures and forward contracts concluded on behalf of customers and on own account. These instruments are booked at their fair value (mark to market).

Gross positive and negative replacement values of derivative instruments open at the balance sheet date are recorded in the corresponding item of the balance sheet.

At closing date, the derivative financial instruments held were primarily for hedging purposes. The gain or loss from the revaluation of hedging positions is taken to the same item in the income statement as the gain or loss from the transaction hedged. For trading positions, resulting gains or losses form part of "Result from trading operations and fair value option".

### 5.2.3.7 Financial investments

Debt securities purchased to be held until maturity are recognised at acquisition cost, with the allocation of premiums and discounts over the duration of the instrument. Any profit or loss resulting from the early disposal of these securities is spread over their residual duration, i.e. until their original maturity. Any value adjustment resulting from the deterioration of the debtor's solvency is booked to the income statement under "Changes in value adjustments for default risk and losses from interest operations".

Fixed-interest-bearing securities acquired in view of subsequent sale before maturity (securities which are not in the trading portfolio) are valued at the lower of their cost or market value. The balance of price changes is included in "Other ordinary expenses" (if the market value is lower than the purchase value) or in "Other ordinary income" (for revaluations up to the acquisition cost). Gains and losses are booked in the income statement under "Result from the disposal of financial investments".

Participations, shares in financial investments, and precious metals are valued at the lower of their cost or market value.

Buildings reacquired by the Bank in connection with lending activities and intended for sale are entered in the balance sheet at the lower of purchase or sale price.

### 5.2.4 Participations

This item comprises company equity stakes, in terms of capital, held as long-term investments.

Non-consolidated participations are recorded at acquisition value less economically necessary depreciation, providing the preconditions for a valuation based on the equity method are not given.

Companies on which a significant influence, but no control, can be exerted are valued according to the equity method. The booked value of the participation is adjusted to the net portion of assets held. Influence is deemed to be significant when the shares range between 20% and 50% of capital with voting rights.

### 5.2.5 Tangible fixed assets

This item includes Group premises, computer hardware and telecommunication equipment, licenses and software, technical facilities, furniture and vehicles.

Depreciation rates are calculated over the estimated useful life as follows:

• land and buildings (masonry)	40 years (up to the official estimated value of the land)
• equipment	15 years
• banking facilities	5 years
• hardware	5 years
• licenses and software	2 years
• furniture	5 years
• works of art	5 years
• vehicles	3 years

Fixed assets which are no longer in use, or under extraordinary depreciation, are written down (impairment of fixed assets). Fixed assets are valued at cost less economically necessary amortization.

Depreciation is calculated by applying a straight-line method which starts when the items are first utilised.

### 5.2.6 Intangible fixed assets

Goodwill is recognised on the balance sheet applying a straight-line depreciation over a 5-year period. An analysis is performed on a yearly basis in order to define the possible need for extraordinary depreciation.

### **5.2.7 Provisions**

This item includes probable commitments whose amounts and/or due date are uncertain but can be reliably estimated. It also comprises a provision for deferred taxes resulting from consolidation activities.

### **5.2.8 Reserves for general banking risks**

In compliance with the FINMA guidelines on financial statement reporting (FINMA Circ. 2015/1 Accounting Rules - banks), the reserves for general banking risks are prudently created reserves set aside to cover latent risks related to banking activities.

As laid down in Art.21c of the Swiss Federal Ordinance on Capital Adequacy and Risk Diversification for Banks and Securities Traders (CAO) such reserves are considered as equity. Only the reserves for general banking risks of the parent company BancaStato are not subject to taxation. Any addition or release is booked in the income statement under "Changes in reserves for general banking risks".

### **5.2.9 Taxes**

Current income and capital taxes are booked in the Income Statement under "Taxes".

### **5.2.10 Commission expenses**

Commission expenses comprise outsourced services connected to payment transactions, securities administration, and stock exchange / forex / treasury back-office for a total amount of CHF 2,011,000 (CHF 2,253,000 in 2016).

### **5.2.11 Off-balance sheet**

Off-balance sheet operations are reported at their nominal value. Individual provisions are made under "Provisions" for any risk of loss.

### **5.2.12 Own debt instruments and equity securities**

Own debt securities and similar instruments are offset against the corresponding liabilities items.

### **5.2.13 Pension benefit obligations**

The Group does not have a pension institute of its own. At the end of the accounting period the Group had no

obligation towards the pension funds. There are no contribution reserves on the part of the employers and the relationships between the Group's banks and their pension funds are based on global affiliation contracts. Within the framework of these contracts, no possibility of under-coverage exists and, consequently, there are no obligations in this regard on the part of the employers.

### **5.2.14 Recording of business transactions**

All transactions concluded by the balance sheet date are recorded daily and evaluated according to accepted accounting principles. The result of all completed transactions is included in the income statement.

### **5.2.15 Treatment of past-due interest**

Interest which is more than 90 days overdue is considered non-performing and is no longer considered as interest income. A provision is recorded and directly offset by assets.

### **5.2.16 Foreign currency translation**

The Group accounts are in Swiss francs.

Assets and liabilities denominated in foreign currency are converted into Swiss francs at the rate of exchange at the balance sheet closing date. Resulting gains or losses are taken to the income statement under "Result from trading operations and fair value".

Proceeds and expenses generated in foreign currency are converted at the exchange rate applicable at the time the individual transactions are entered or the single economic flows are effected.

Maturing proceeds and maturing expenses (pro-rata) are accounted for in the income statement at the exchange rate applicable at the balance sheet closing date.

Exchange rates applied at the end of the financial year for the major currencies were as follows:

EUR/CHF 1.1703 (2016: 1.0724)

USD/CHF 0.9747 (2016: 1.0158)

### **5.2.17 Treatment of the refinancing of trading positions**

In 2017, income from interest and dividend from the trading portfolio is offset against refinancing costs of the trading portfolio.

## 5.2.18 Consolidation principles

### 5.2.18.1 Consolidation perimeter

Banks and finance companies in which BancaStato directly or indirectly holds a majority of voting rights or capital, or in which it has a controlling interest, are consolidated by the full consolidation method.

Minority participations (i.e. below 20%) or participations in non-financial activities, as well as participations held solely with a view to their future disposal, are excluded from the consolidation perimeter and are evaluated at their purchase value less appropriate depreciation. If the participation share is comprised between 20% and 50% of voting rights, the evaluation is based on the equity method.

### 5.2.18.2 Consolidation method

Capital is consolidated following the purchase method. Acquisition costs of the stake are offset by existing equity at the time of purchase. Any goodwill is recognised on the balance sheet under "Intangible assets" and depreciates over a five-year period. Conversely, any negative goodwill (badwill) is immediately booked in the income statement under "Extraordinary income" if it is an authentic "lucky buy", while outflows of future resources are booked in the balance sheet under "Other liabilities". An impairment test is performed annually. Should this test reveal that an asset value is no longer justified, additional amortisations would be effected at that time.

In the case of partial equity participation, the "minority interests" of the other participants, both in terms of capital participation and share in yearly results, would be shown on the balance sheet.

Following the full consolidation method, the amounts of all balance sheet, off-balance sheet and income statement items of the subsidiaries are aggregated with the corresponding amounts of the Parent Bank's balance sheet, off-balance sheet and income statement.

Transactions between the various entities within the Group annul each other out.

### 5.2.18.3 Consolidation period

The consolidation period corresponds to the calendar year beginning 1 January and ending 31 December. Acquisitions effected during the year are included in the income statement from the date of purchase. The statutory end-year closing for all Group entities is 31 December.

## 5.3 ADJUSTMENT OF THE ACCOUNTING PRINCIPLES FOR THE PRESENTATION OF FINANCIAL STATEMENTS

There were no changes in accounting principles in 2017.

## 5.4 RISK MANAGEMENT

The Group, like any other financial institute, is subject to various banking-specific risks, namely credit, market, liquidity and operational risks.

Risk management is a priority for the Group. Its goal is to identify, measure and monitor banking risks in order to preserve the Group's assets and to enhance profitability.

Risk management is defined in the Group's Rules and Regulations as well as in the Rules and Regulations of the single legal entities, and is reviewed annually. The Group's Rules and Regulations define the parameters the single legal entities must abide by.

The key elements of risk management are:

- a comprehensive risk policy;
- the use of recognized risk measurement and risk management principles;
- the definition of various risk limits for each type of risk and the ongoing monitoring of compliance to these limits;
- timely and comprehensive reporting;
- the allocation of adequate financial, technical and human resources to risk management;
- emphasis on risk awareness and promoting a risk-sensitive corporate culture at all staff levels.

The Board of Directors exercises the ultimate responsibility, supervision and control and is therefore the supreme organ for managing risk. It defines the key elements of risk management. The Executive Board is responsible for implementing the Board of Directors' policies. In particular, it is the Executive Board's duty to ensure that a suitable risk management process is in place and that an effective risk monitoring system is activated. This includes the implementation of an organisation for its supervision at the consolidated level, and as regards outsourced activities.

Risk is identified, measured and monitored by operationally independent units that report to the Executive Board, which in turn reports to the Board of Directors on a regular basis.

An information system ensures that the members of the Board of Directors as well as the Executive Board are updated regularly regarding the Bank's and the Group's asset and financial position, as well as on the meeting of set targets and risks incurred.

Both the Board of Directors and the Executive Board periodically analyse, within their own area of expertise, the information received as regards credit, market, liquidity and operational risks.

In its meeting of 26 April 2017, the Audit and Risk Committee of the Board of Directors of the Parent Bank and, subsequently, the Board of Directors of the Parent Bank in its meeting of 28 April 2017, assessed the Group's risk profile.

In this regard, the Board of Directors annually reviews the applicable legislation and "level of accepted risk". Capital and liquidity planning is prepared annually for a minimum period of three years.

#### 5.4.1 Credit risk

Credit risk stems from the inability of a counterparty to fulfil its contractual obligations, or from the reduced value of collateral or financial instruments issued by a third party (value of equity-type securities, interest rate instruments, shares in collective capital investments) due to the worsening of its financial standing.

The Group's exposure to credit risk is primarily linked to lending activities, mostly mortgage, commercial and Lombard loans granted to clients.

BancaStato operates essentially in the local market of Ticino and only marginally in other Cantons and abroad. Axion Swiss Bank SA operates primarily by granting of Lombard loans to its clients.

Credit risk is managed by setting prudent lending margins on collateral and credit granting procedures at different hierarchical levels on the basis of the aggregate amounts granted and risk incurred.

Procedures for the delegation of competences on the part

of the Board of Directors, as well as the specific internal organisational structure, ensure that the units that assume risk are independent from those that manage risk.

The Board of Directors is responsible for approving large credit exposures as well as loans to members of the governing bodies. At BancaStato, other loan granting competencies are entrusted to the Credit Risk Committee, and at Axion to the Executive Board who may delegate some *ad personam*. The Credit Risk Committee is composed of three members of the Executive Board, the Head of Credit Management and Analysis or a Credit Officer. This Committee deals with all credit matters delegated to it and draws up notices to the Board of Director for decisions falling within the Board's competence. In addition, at BancaStato, competencies are delegated to Credit Officers who are independent of client advisory units. Still at BancaStato, the specific authority to grant loans involving low risk profiles is delegated to client advisers. However, such loans may be granted only within the limits of the predefined parameters used in the IT-based decision-making process. An internal control system ensures loan granting processes and competency delegation rules are complied with. Loans reviewed and approved by the competent authorities are managed by the Credit Competence Center which is independent of client advisers and credit officers.

Credit risk management and monitoring are defined in the Banks' lending regulations. These state that the Group's Banks assume credit risk only after an in-depth analysis of the operation, including a review of credit-worthiness, transaction structure, integrity of the counterparties and collateral has been carried out. Each credit application is treated on the basis of standardised criteria set within each institute. Lending regulations are reviewed annually and supplemented by internal directives and operational manuals.

To assess creditworthiness, the Group's Banks refer to external ratings prepared by first-class rating agencies when available. BancaStato also utilises a rating model for granting mortgage and business loans to its private and commercial clients. The rating model ensures a classification of clients based on standard criteria divided into 10 rating classes, assigning a probability of default to each counterparty. This rating is used to determine borrowing capacity as well as to define the interest rate on the loan as a function of risk.

Credit exposure to counterparties are restricted by credit limits.

Sustainability calculation procedures are regulated by internal rules and regulations. The maximum loan amount granted to businesses is determined on the basis of a calculation of their financing potential which, in turn, is closely linked to the durable income (cash flow) that the business is able to generate to remunerate debt capital. This same sustainability (cash flow over capital) principle is applied to calculate loans to private clients. In particular, sustainability calculations for mortgage loans are performed by comparing durable available income with expenses (i.e. interests, loan amortisation and maintenance costs).

Maximum loan values are set for each type of collateral on the basis of common banking standards. The maximum amount for a mortgage loan is established based on the debtor's ability to pay and on the value of the real estate being mortgaged. The valuation principles applied to collateral are described in the Section 5.6 "Valuation of collateral". For Lombard loans, the assigned limit is determined on the basis of a foreseeable value of pledged assets which are revalued at market value on a daily basis.

The Group's Rules and Regulations and the Banks' Rules and Regulations set the limits within which the various Group entities are authorised to assume a country risk.

The credit risk on financial instruments owned by the Group's Banks is managed by adhering to product, diversification and quality restrictions as established by the Board of Directors.

Interbank business, which is derived from client and own business, is carried out within a predefined limit system with primary Swiss and international banks. The maximum amount set depends on the counterparty's solvency which is constantly monitored. Counterparty limits are reviewed at least once a year. The compliance to these limits is monitored by business units which are independent from risk assuming units.

Concentration risk is monitored by the Risk Management unit and results are submitted to the Executive Board and the Board of Directors. The Group undertakes periodic stress tests in relation to its own credit risk concentration.

The Executive Board and the Board of Directors are provided on a regular basis with updated information on the risk profile of the loan portfolio.

#### **5.4.2 Interest rate risk**

As the Group is heavily involved in balance sheet transactions, interest rate risk may have a significant impact on the interest margin. The Group's exposure to rate risk is primarily due to the time lapse between fundraising and application. The measurement and control of risk resulting from this imbalance are of primary importance to any bank. This task is part of the assets & liabilities management (ALM) performed by BancaStato's ALCO, which is composed of members of the Executive Board, the Head of Treasury and the Head of Financial and Risk Management, as well as the Axion Risk Committee.

As regards the ALM activity, the Group's risk policy, as approved by the Board of Directors, defines the modes of operation and limitations, and regulates risk monitoring. The rate risk related to balance and off-balance sheet operations is managed and monitored centrally by the ALCO which was assigned operational limits. Operations at Axion are managed by its Risk Committee. Competencies are determined in terms of changes in current equities for a 1% sudden parallel shift in market rates (value effect) and a movement in interest margin in the following 12 months still with the same market parameter variations (income effect). On the basis of the chosen methodology, monitoring refers to the present value of equity and to the variation of net interest income in the 12 months following measurement. A software feature enables Risk Management to regularly provide the ALCO and Axion's Risk Committee with information on risk exposure, simulations of the interest margin, as well as to perform stress tests, i.e. analyses based on predetermined potentially negative scenarios.

For the management of the rate risk inherent to variable rate products without fixed maturity, replication models are used to assess such risk. These models take into consideration both the correlation with the evolution of interest rates and the impact on balance sheet volumes as a result of client behaviour.

To cover or mitigate exposure to interest rate risk, hedging derivative instruments may be used (these are substantiated to match the hedged item, and their effectiveness is periodically monitored by Risk Management).

The "treasury" function guarantees long-term refinancing and manages the interest rate risk by taking into account the Bank's

objectives, i.e.:

- record, measure and manage all interest rate risks arising from client transactions with the Bank;
- generate risk-adjusted income within the risk limits;
- ensure cost-effective refinancing in line with the development of the balance sheet;
- monitor liquidity and avoid potential liquidity shortfalls.

### 5.4.3 Other market risks

#### 5.4.3.1 Currency risk

The Group's currency risk management serves to minimise any negative impact on its earnings due to interest rate changes. Basically, the goal is to balance the assets denominated in foreign currencies with the liabilities in the same currency. This exposure is under constant monitoring.

#### 5.4.3.2 Trading operations

The Group's exposure to other market risks arises from trading operations which are limited and mostly in relation to client requirements. In this respect, prudent limits of maximum exposure have been established based on the asset value at risk (position and loss limits). The Group does not engage in market making activities. The limits for trading positions are verified daily by Risk Management.

The Risk Management unit submits to the Executive Board, on a regular basis, detailed information on exposures and compliance to the set limits. The latter subsequently informs the Board of Directors.

#### 5.4.4 Liquidity risk

Liquidity risk is managed and monitored actively by setting a minimum reserve of liquidity, a system of limits and indicators, diversification of refinancing (source, currencies and durations) and the implementation of stress scenarios. In fact, the internal policy regarding liquidity risk prescribes that the Group must have available the needed liquidity on a permanent basis to fulfil its own payment commitments, even in stress situations, as

well as comply with the applicable banking provisions.

The ALCO manages liquidity and draws up the strategy, the limits and the objectives in compliance with the mandate received by the Board of Directors. Operations at Axion are managed by its Risk Committee. The treasury function guarantees that limits and objectives are adhered to. The Risk Management unit monitors liquidity, the financing situation and concentration risks.

The emergency liquidity plan is a key aspect of the crisis management plan. It includes intervention measures to counter any liquidity crisis, taking into account liquidity indicators and ratios, and outlining emergency procedures.

#### 5.4.5 Operational risk

Operational risk is directly related to banking operations and includes the possibility of direct or indirect losses resulting from inadequate or incorrect internal processes, inappropriate business conduct on the part of individuals, system malfunctions or external events. Operational risk also comprises legal and compliance risks.

The management of operational risk consists primarily in the adoption of risk mitigating measures aimed at eliminating or reducing risk as much as possible.

In-house rules and guidelines define the organisation of work and limit the extent of such risk. An appropriate system of controls at various levels, as well as specific structures designed to oversee the application of established rules and procedures have been implemented so as to limit the exposure to operational risk. Key controls are documented in a standardised manner.

The Legal and Compliance Department is responsible for verifying the adherence to applicable regulatory provisions, as well as due diligence duties. It also ensures that the internal guidelines are continually being adapted to new legal and regulatory provisions.

The Security Service sets up appropriate organisational and technical measures in order to mitigate risks related to external and internal events or actions (natural occurrences, criminal acts of any kind, both physical and IT-related). This service also

prepares and regularly updates a corporate continuity plan.

The Parent Company records and analyses all information on occurrences of operational malfunction which result in a financial impact (gain and loss) and classifies these data on the basis of standardised criteria. The frequency, seriousness and causes of the various events are duly assessed, and corrective measures implemented as needed. Periodic reporting to the Group's authorities is carried out by independent units.

The Banks perform periodic reviews of internal control procedures during which they assess the operational effectiveness of control with regard to existing risks, implementing improvement measures as needed.

The Group invests in training staff and in the promotion of risk-awareness, particularly for those employees who are in direct contact with customers.

The Group has established a specific organization and defined processes and responsibilities in order to oversee the providers of outsourced services.

Every month, "Risk Management", "Internal Control", "Security", "Human Resources", "Service Center" and "Legal and Compliance" submit to the Parent Company's Risk Committee their findings resulting from the internal priority control system within the various Group entities along with a summary notice on major risks. The Risk Committee is responsible for ensuring appropriate surveillance of overall risks and particularly operational risks. A condensed analysis of information on major operational risk is forwarded to the Board of Directors.

## **5.5 METHODS USED FOR IDENTIFYING DEFAULT RISK AND DETERMINING THE NEED FOR VALUE ADJUSTMENTS**

Credits are monitored in a differentiated manner according to established procedures based on the risk profile of exposures.

In order to guarantee the periodic and seamless monitoring of all assumed credit risks, all credit facilities must be renewed. Credit monitoring is performed through a variety of periodic analysis carried out by the responsible client adviser, the Credit Office and the Recovery and Repositioning unit with the aim of identifying any sign of reduced creditworthiness, and forestalling circumstances which might impair loans or require action to reduce risk. The prerequisites for the renewal of credit facilities are modelled on those for the granting of new loans. The results

of these periodic analyses determine whether the limit can be maintained or requires adjustments.

The renewal conditions are established for each individual loan based on the type of client and product, as well as the collateral and loan characteristics. Moreover, each loan will be subject to a fresh review in those circumstances affecting the debtor's solvency or if the debtor is more than 90 days overdue in interest, amortisation or commission payments or is unable to fully reimburse capital (non-performing loan).

Non-performing or impaired loans that have been granted by BancaStato are monitored by "Recovery and Repositioning", a designated organisational unit specialising in recovery which is independent of client interface.

Outstanding loans and value of collateral for securities-based loans are monitored daily. If the collateral value of the securities falls below the amount of the credit line, the amount of the loan is either reduced or additional collateral is requested. In the absence of a settlement, the securities are utilised, and the credit position is closed out.

Non-performing and impaired loans are assessed individually, considering existing collateral at its liquidation value. Any risk of default is provisioned individually. The provision represents the expected loss with the counterparty with regard to the corresponding transaction. The organisational unit proposing the loan is responsible for setting any necessary provisions which will be decided upon by the Credit Office or the Executive Board. Similarly, the Recovery and Repositioning unit which is in charge of litigation procedures at BancaStato is tasked with proposing adequate provisions or adjustments with regard to the credits it was entrusted with.

BancaStato's ALCO and Axion's Investment Committee monitor the risk of loss in the financial investment portfolio on the basis of market values or specific analyses.

Portfolio analyses, along with stress tests performed by Risk Management, are used to identify any possible risk of loss present in the loan portfolio.

## **5.6 VALUATION OF COLLATERAL**

### **5.6.1 Mortgage-based loans**

Only BancaStato grants mortgage-based loans.

An up-to-date valuation of the collateral exists for each loan

which is secured by real estate. Real estate pledged as loan collateral is re-evaluated periodically.

Both the characteristics of the asset pledged, and its present and future economic use are taken into account in the appraisal of real estate. As a general rule, the valuation is based on market value, an amount corresponding to the price that may be obtained within a period of one year under normal market conditions as a result of offer and demand.

Owner-occupied residential properties are evaluated, within specified limits, with the help of hedonic valuation models that compare property transactions data on the basis of the detailed characteristics of each property.

In the case of multi-family housing, commercial buildings and special properties, internal real estate appraisers, as well as any external certified appraiser, calculate these values amongst others by taking into consideration rental income. If the credit rating is low, a liquidation value is calculated.

The lowest value resulting from the internal valuation, purchase price and any external estimate, defines the value of the pledged collateral.

Properties pledged as collateral against impaired loans are estimated at their liquidation value.

### 5.6.2 Securities-based loans

In general, transferable financial instruments (such as bonds and shares) that are liquid and actively traded, are accepted for Lombard loans and other securities-based loans. Similarly, transferable structured products for which there is regular market information and a market maker, are also accepted.

To calculate the value of liquid and negotiable securities, the Banks apply a discount to the market value in order to cover the market risk associated with these securities. Discounts may vary depending upon the type of product, the counterparty's rating, the residual duration of the financial instrument and the currency. The discounts used for structured products are higher than those for liquid securities. For life insurance policies or bank guarantees, these discounts are determined on the basis of the product and counterparty.

## 5.7 BUSINESS POLICY REGARDING THE USE OF DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGE ACCOUNTING

Derivative financial instruments are used for trading and hedging purposes.

Derivative financial instruments are traded exclusively by specially trained traders. The Group's Banks do not act as market makers. Trading is undertaken both with standardised and OTC instruments on own account and on behalf of clients, especially interest-, currency-, equity-/index-based instruments. There is no trading in credit derivatives.

Derivative financial instruments are principally used in risk management to hedge interest rate and currency risks.

In general, recognition in the income statement of the result of a hedging transaction follows the same principles applied to the secured underlying. As a consequence, results from hedging operations with derivative financial instruments within the framework of the structural management of the balance sheet are booked on a *pro rata* basis (accrual method).

If the impact of a hedging transaction exceeds that of the hedged items, the excess fraction of the derivative instrument is considered as a trading transaction. This revaluation is booked under "Results from trading operations and fair value option".

The use of interest rate swaps (IRS) in the structural management of the balance sheet serves to hedge rate variations or changes in present values of specific items. Primarily plain vanilla swaps, both payer and receiver, may be used. In general, receiver swaps are used to hedge specific individual fixed rate items in liabilities and are therefore considered micro hedges. On the other hand, portfolio items or fixed rate positions under assets are hedged through payer swaps and are therefore considered macro hedges.

Short term interest rate swaps and tom next / overnight interest rate swaps are used to manage the gap between assets and liabilities with maturities below 12 months as well as for the current management of liquidity.

Treasury swaps are used within the framework of the structural management of the balance sheet in order to manage currency risk resulting from the conversion of the available liquidity in foreign currency into Swiss francs or from the need to refinance loans in foreign currency. This instrument is used as an alternative to either an interbank investment in foreign currency

of excess liquidity, particularly in the case of uncertainty with regard to the quality of foreign counterparts or interbank refinancing in foreign currency. With a treasury swap, the Bank can transform excess liquidity in foreign currency into Swiss francs, for a fixed period, thus enabling its placement in domestic currency without incurring an exchange rate risk or convert excess liquidity in domestic currency into foreign currency in order to finance loans in foreign currency.

Spot exchange, forward forex and currency options are used within the framework of the structural management of the balance sheet to hedge currency risk on economic flows (whether interest margins or commissions) in foreign currency.

## 5.8 MATERIAL EVENTS AFTER THE BALANCE SHEET DATE

No major event occurred after the balance sheet date that would have a decisive impact on assets, the financial position or the income of the Group as at 31 December 2017.

## 5.9 REASONS WHICH HAVE LED TO EARLY RESIGNATION OF THE AUDITORS

PricewaterhouseCoopers AG, Lugano were designated as External Auditors for the Group, and are still in office.

## 5.10 INFORMATION ON THE BALANCE SHEET

### 5.10.1 Securities financing transactions (assets and liabilities)

(CHF thousands)	31.12.2017	31.12.2016
<b>Securities lending, securities borrowing and repurchase agreements</b>		
Book value of receivables from cash collateral delivered in connection with securities borrowing and reverse repurchase transactions <sup>1</sup>	-	-
Book value of obligations from cash collateral received in connection with securities lending and repurchase agreements <sup>1</sup>	70,000	125,000
Book value of securities lent in connection with securities lending or delivered as collateral in connection with securities borrowing as well as securities in own portfolio transferred in connection with repurchase agreements	68,641	122,804
<i>of which with unrestricted right to resell or repledge</i>	<i>68,641</i>	<i>122,804</i>
Fair value of securities received and serving as collateral in connection with securities lending or securities borrowed in connection with securities borrowing as well as securities received in connection with reverse repurchase agreements with an unrestricted right to resell or repledge	-	-
<i>of which repledged</i>	<i>-</i>	<i>-</i>
<i>of which resold</i>	<i>-</i>	<i>-</i>

<sup>1</sup> Before any netting agreement.

### 5.10.2 Presentation of collateral for loans / receivables and off-balance sheet transactions, as well as impaired loans / receivables at 31.12.2017

(CHF thousands)	Type of collateral			
	Secured by mortgage	Other collateral	Unsecured	Total
<b>Loans (before netting with value adjustments)</b>				
Amounts due from customers	170,968	481,808	576,457	1,229,233
Amounts due from public corporations	61	692	686,402 <sup>1</sup>	687,155
Mortgage loans	8,853,705 <sup>1</sup>			8,853,705
<i>Residential property</i>	6,560,497			6,560,497
<i>Office and business premises</i>	1,135,964			1,135,964
<i>Commercial and industrial premises</i>	477,407			477,407
<i>Other</i>	679,837			679,837
<b>Total loans (before netting with value adjustments)</b>	<b>9,024,734</b>	<b>482,500</b>	<b>1,262,859</b>	<b>10,770,093</b>
Previous year	8,459,387	490,949	1,177,926	10,128,262
<b>Total loans (after netting with value adjustments)</b>	<b>9,003,841</b>	<b>475,674</b>	<b>1,228,528</b>	<b>10,708,043</b>
Previous year	8,434,588	484,069	1,154,551	10,073,208
<b>Off-balance sheet</b>				
Contingent liabilities	7,033	61,767	71,281	140,081
Irrevocable commitments	1,882	11,331	36,400 <sup>2</sup>	49,613
Obligations to pay up shares and make further contributions	-	-	14,180	14,180
<b>Total off-balance sheet</b>	<b>8,915</b>	<b>73,098</b>	<b>121,861</b>	<b>203,874</b>
Previous year	29,608	71,700	121,706	223,014

(CHF thousands)	Gross debt amount	Estimated liquidation value	Net debt amount	Individual value adjustments
<b>Impaired loans</b>				
<b>Current year</b>	<b>158,429</b>	<b>96,379</b>	<b>62,050</b>	<b>62,050</b>
<i>of which with collateral</i>	121,918	94,199	27,719	27,719
<i>of which unsecured</i>	36,511	2,180	34,331	34,331
Previous year	129,079	74,025	55,054	55,054
<i>of which with collateral</i>	102,349	70,671	31,678	31,678
<i>of which unsecured</i>	26,730	3,354	23,376	23,376

<sup>1</sup> Including loans to entities related to public institutions for CHF 136.4 million (2016: 134.9 million).

<sup>2</sup> Including CHF 35 million (2016: CHF 34.1 million) as a required share for deposit guarantee purposes.

### 5.10.3 Breakdown of trading portfolios and other financial instruments at fair value

(CHF thousands)	31.12.2017	31.12.2016
<b>Trading portfolio assets</b>		
Debt securities, money market securities	2,269	1,363
<i>of which listed</i>	2,269	1,363
Equity-type securities	121	363
Shares in investment funds	18,388	10,988
Precious metals and commodities	20,055	15,079
<b>Total trading portfolio assets</b>	<b>40,833</b>	<b>27,793</b>
<i>of which determined using a valuation model</i>	-	-
<i>of which securities eligible for repo transactions in accordance with liquidity requirements</i>	-	-

### 5.10.4 Presentation of derivative financial instruments (assets and liabilities)

(CHF thousands)	Trading instruments			Hedging instruments		
	Replacement values		Contract volume	Replacement values		Contract volume
	positive	negative		positive	negative	
<b>Interest rate instruments</b>						
IRS	-	-	-	6,986	17,341	534,000
Options (OTC)	-	-	-	-	-	-
<b>Total interest rate instruments</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>6,986</b>	<b>17,341</b>	<b>534,000</b>
<b>Foreign currencies / precious metals</b>						
Forward contracts	744	643	87,742	-	101	26,348
Combined currency and interest rate Swaps	3,579	3,661	443,219	39,006	5,625	2,091,065
Options (OTC)	1,292	1,292	185,808	-	-	-
<b>Total foreign currencies / precious metals</b>	<b>5,615</b>	<b>5,596</b>	<b>716,769</b>	<b>39,006</b>	<b>5,726</b>	<b>2,117,413</b>
<b>Total before netting agreements</b>	<b>5,615</b>	<b>5,596</b>	<b>716,769</b>	<b>45,992</b>	<b>23,067</b>	<b>2,651,413</b>
<i>of which determined using a valuation model</i>	<i>5,615</i>	<i>5,596</i>	<i>-</i>	<i>45,992</i>	<i>23,067</i>	<i>-</i>
Total previous year	7,161	6,913	682,549	16,908	45,377	2,996,976
<i>of which determined using a valuation model</i>	<i>7,161</i>	<i>6,913</i>	<i>-</i>	<i>16,908</i>	<i>45,377</i>	<i>-</i>
	Positive replacement values (cumulative)		Negative replacement values (cumulative)			
<b>Total after netting agreements</b>	<b>51,607</b>		<b>28,663</b>			
Total previous year	24,069		52,290			

### Breakdown by counterparty

(CHF thousands)	Central clearing houses	Banks and securities dealers	Other customers
Positive replacement values (after netting agreements)	-	49,596	2,011

No netting contracts existed on outstanding derivative financial instruments at 31.12.2017 and 31.12.2016.

### 5.10.5 Breakdown of financial investments

(CHF thousands)	Book value		Fair value	
	31.12.2017	31.12.2016	31.12.2017	31.12.2016
Debt securities	257,209	266,079	258,854	267,946
<i>of which intended to be held to maturity</i>	257,209	266,079	258,854	267,946
<i>of which not intended to be held to maturity (available for sale)</i>	-	-	-	-
Shares in investment funds	26,885	27,616	27,696	27,787
Equity-type securities	9,830	207	10,261	405
<i>of which qualified participations (at least 10% of voting capital)</i>	-	-	-	-
Precious metals	126	146	126	146
Real estate	1,363	1,450	1,363	1,450
<b>Total financial investments</b>	<b>295,413</b>	<b>295,498</b>	<b>298,300</b>	<b>297,734</b>
<i>of which securities eligible for repo transactions in accordance with liquidity requirements</i>	153,502	144,091	154,953	146,322

### Breakdown of counterparties by rating

(CHF thousands)	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	Below B-	Unrated
Book value of debt securities	178,774	29,563	28,233	401	-	20,238

The valuations of debt securities are based on ratings by Standard & Poor's.

### 5.10.6 Presentation of participations

(CHF thousands)	Acquisition cost	Accumulated value adjustments and/or changes in book value (equity method)	Book value 31.12.2016	Reclassifications	2017				Book value 31.12.2017	Market value
					Additions	Disposals	Value adjustments	Changes in book value of participations valued using the equity method / depreciation reversals		
Participations valued using the equity method										
listed	-	-	-	-	-	-	-	-	-	-
unlisted	400	117	283	-	-	-	-	40	323	-
Other participations										
listed	-	-	-	-	-	-	-	-	-	-
unlisted	14,684	8,578	6,106	-	100	-	-	-	6,206	-
<b>Total participations</b>	<b>15,084</b>	<b>8,695</b>	<b>6,389</b>	<b>-</b>	<b>100</b>	<b>-</b>	<b>-</b>	<b>40</b>	<b>6,529</b>	<b>-</b>

## 5.10.7 Disclosure of companies in which the Bank holds a permanent or indirect significant participation

Companies are recognized on the basis of the full consolidation method.

Company name	Head office	Business activity	Company capital (CHF thousands)	Share of		Held	
				capital in %	votes in %	direct	indirect
AHSA Holding SA	Lugano	Financial company	0 <sup>1</sup>	100.0%	100.0%	100.0%	-
Axion SWISS Bank SA	Lugano	Banking	43,000	100.0%	100.0%	100.0%	-

The companies hereunder are valued using the equity method

Company name	Head office	Business activity	Company capital (CHF thousands)	Share of		Held	
				capital in %	votes in %	direct	indirect
Londinium Dac	Dublin	Investment company (refer to MiFID)	176 <sup>2</sup>	30.0%	30.0%	30.0%	-
Soave Asset Management Ltd	Lugano	Asset management company	216 <sup>2</sup>	30.0%	30.0%	30.0%	-

### Participations recorded in the balance sheet under "Financial investments"

Company name	Head office	Business activity	Company capital (CHF thousands)	Share of		Held	
				capital in %	votes in %	direct	indirect
Geneva Cantonal Bank	Geneva	Banking	360,000	0.01%	0.01%	0.01%	-
Swiss National Bank	Bern		25,000	0.10%	0.10%	0.10%	-

### Participations recorded in the balance sheet under "Participations"

Company name	Head office	Business activity	Company capital (CHF thousands)	Share of		Held	
				capital in %	votes in %	direct	indirect
<b>Financial and services companies held with cantonal banks</b>							
Adungi Holding SA	Zurich	Financial company	25,000	0.40%	0.40%	0.40%	-
Caleas SA	Zurich	Financial company	800	2.24%	2.24%	2.24%	-
Central mortgage bond institution of SCB	Zurich	Mortgage bond issuing institution	1,625,000	1.09%	1.09%	1.09%	-
Newhome.ch AG	Zurich	Real estate portal	100	5.40%	5.40%	5.40%	-
<b>Financial and services companies held with Swiss banks</b>							
SIX Group AG	Zurich	Service company	19,500	0.15%	0.15%	0.15%	-
Swiss Bankers Prepaid Services SA	Grosshöchstetten	Financial company	10,000	0.20%	0.20%	0.20%	-
<b>Other participations</b>							
Alloggi Ticino SA	Bioggio	Real estate company	15,200	2.11%	2.11%	2.11%	-
Autosilo Piazza del Sole SA	Bellinzona	Car park	2,000	10.0%	10.0%	10.0%	-
Swiss Hotel Credit Society	Zurich	Financial company	28,457	1.32%	1.32%	1.32%	-
Teleticino SA	Melide	Radio and television productions	4,950	23.15%	16.98%	16.98%	-
Centro Sci Nordico Campra SA	Blenio	Real estate company	1,550	6.40%	6.40%	16.40%	-

<sup>1</sup> The capital of AHSA Holding SA was reimbursed, but cancellation from the Commerce Registry of Canton Ticino is still pending.

<sup>2</sup> Sale-purchase contracts associated with participations in Soave Asset Management Ltd. and Londinium Dac grant the Bank the right to sell both participations by 2019. Should the Bank not make use of this right, both vendors may reacquire these participations in 2019. In the event the Bank does not exercise its right to sell, or the vendors their right to repurchase, the Bank may exercise, in 2019, its purchase right of a further 21% of participation share in both companies. If the Bank exercises this right, the vendors will be entitled to sell the remaining 49% share.

### 5.10.8 Presentation of tangible fixed assets

(CHF thousands)	Acquisition cost	Accumulated depreciation	Book value 31.12.2016	2017					Book value 31.12.2017
				Reclassifications	Additions	Disposals	Depreciation	Reversals	
Bank buildings	177,549	117,336	60,213	-	2,139	-	4,021	-	58,331
Other real estate	26,773	12,848	13,925	-	-	-	552	-	13,373
Acquired software	81,286	76,629	4,657	-	3,281	-	3,635	-	4,303
Other tangible fixed assets	107,147	103,542	3,605	-	1,610	-	1,111	-	4,104
<b>Total tangible fixed assets</b>	<b>392,755</b>	<b>310,355</b>	<b>82,400</b>	<b>-</b>	<b>7,030</b>	<b>-</b>	<b>9,319</b>	<b>-</b>	<b>80,111</b>

### 5.10.9 Presentation of intangible assets

(CHF thousands)	Cost value	Accumulated amortisation	Book value 31.12.2016	2017					Book value 31.12.2017
				Reclassifications	Additions	Disposals	Amortisation	Reversals	
Goodwill	37,077	15,713	21,364	-	-	-	7,062	-	14,302
<b>Total intangible assets</b>	<b>37,077</b>	<b>15,713</b>	<b>21,364</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>7,062</b>	<b>-</b>	<b>14,302</b>

### 5.10.10 Breakdown of other assets and other liabilities

(CHF thousands)	31.12.2017	31.12.2016
<b>Other assets</b>		
Compensation account	6,365	11,747
Indirect taxes	637	857
Various other assets	10,772	266,069 <sup>1</sup>
<b>Total other assets</b>	<b>17,774</b>	<b>278,673</b>
<b>Other liabilities</b>		
Direct/indirect taxes	5,174	6,154
Unredeemed cash bonds	2,312	2,903
Compensation account	737	-
Various other liabilities	117,712 <sup>2</sup>	2,726
<b>Total other liabilities</b>	<b>125,935</b>	<b>11,783</b>

<sup>1</sup> of which a balance of CHF 261 million resulting from in-house banking operations.

<sup>2</sup> of which CHF 91.1 million from in-house banking operations and CHF 23.4 million additional payment to the Canton for 2016.

### 5.10.11 Disclosure of assets pledged or assigned to secure own commitments and of assets under reservation of ownership

(CHF thousands)	31.12.2017		31.12.2016	
	Book value	Effective commitments	Book value	Effective commitments
<b>Pledged / assigned assets</b> (excluding advances and repurchase agreements with securities)				
Book value of mortgages set as collateral for bonds and loans with the SCB Central	2,501,045	2,042,000	2,450,430	1,968,000
Book value of securities delivered as collateral to SIX Group AG	1,417	-	1,818	-
Book value of securities delivered as collateral in connection with Repo Light credit with SNB	23,503	-	22,325	-
Book value of assets pledged to secure own commitments	11,315	9,363	12,554	10,701
<b>Total pledged / assigned assets</b>	<b>2,537,280</b>	<b>2,051,363</b>	<b>2,487,127</b>	<b>1,978,701</b>
<b>Assets under reservation of ownership</b> Assets under reservation of ownership	-	-	-	-

### 5.10.12 Disclosure of the economic position of own pension schemes

#### 5.10.12.1 Disclosure of liabilities relating to own pension schemes, and number and nature of equity instruments of the Bank held by own pension schemes

The Group has no obligations towards pension schemes.

#### 5.10.12.2 Disclosures on the economic situation of own pension schemes

##### a) Employer contribution reserves (ECR)

There were no employer contribution reserves as at 31.12.2017.

##### b) Economic benefit / obligation and pension expenses

	Over / underfunding at the end of 2017	Economic interest of the Bank		Change in economic interest and/or commitment versus previous year	Contributions paid for 2017	Pension expenses in personnel expenses	
		31.12.2017	31.12.2016			31.12.2017	31.12.2016
<b>BancaStato</b> Pension plans without over- / underfunding	-	-	-	-	7,725	7,778	6,026
<b>Axion Swiss Bank</b> Pension plans with overfunding	11.3%	-	-	-	938	1,091	1,079

Contributions are paid to the insurance company. The employer's contributions are carried under "Personnel expenses".

BancaStato has opted for affiliation to the Group Plan LPP Swiss Life, a legally independent pension fund. The pension plan is a defined-contribution scheme and provides the basic compulsory coverage as stated in the Swiss LPP (Federal Law on Occupational Benefits), as well as complementary coverage.

Axion Swiss Bank SA provides coverage for all its employees through the Vita Joint Foundation from "Zurich". In its last communication (31.12.2017) this collective scheme coverage ratio amounted to 111.3% based on Art. 44/2 OPP 2 (31.12.2016: 108.3%).

No economic liabilities or economic benefits towards the staff pension scheme existed at year end. The Vita Joint Foundation did not hold any reserves pertaining to employers' contributions for the Bank.

As of 1.1.2018 the pension scheme will be transferred to "LPP Swiss Life Joint Foundation".

At the end of the accounting period the Group had no obligation towards the pension funds. There are no contribution reserves on the part of the employers and the relationships between the Group's banks and their pension funds are based on global affiliation contracts.

The pension funds reinsure all pension risks by means of a comprehensive insurance contract. Within the framework of these contracts, no possibility of under-coverage exists and, consequently, there are no obligations in this regard on the part of the employers.



### 5.10.13 Presentation of bonds outstanding, mortgage bonds from central issuing institutions and mandatory convertible bonds

#### 5.10.13.1 Presentation of bonds outstanding, mortgage bonds from central issuing institutions and mandatory convertible bonds

(CHF thousands)				
Interest rate	Type of bond	Issue year	Due date	Net amount
3.75%	Subordinated without PONV clause <sup>1</sup>	2011	15.12.2021	175,000
0.00%	Non-subordinated <sup>2</sup>	2016	04.03.2022	50,000
0.50%	Non-subordinated <sup>2</sup>	2015	24.06.2024	150,000
0.30%	Non-subordinated <sup>2</sup>	2017	15.06.2027	200,000
<b>Total bonds</b>				<b>575,000</b>
Bonds and loans from central issuing institutions <sup>3</sup>				2,042,000
<b>Total outstanding bonds and mortgage bonds from central mortgage bond institutions and mandatory convertible bonds</b>				<b>2,617,000</b>

<sup>1</sup> Early repayment only under certain conditions.

<sup>2</sup> No early repayment.

<sup>3</sup> Average interest rate 1.06%.

### 5.10.13.2 Overview of maturities of bonds and mortgage bonds from central issuing institutions and mandatory convertible bonds

(CHF thousands)	Within one year	> 1 - ≤ 2 years	> 2 - ≤ 3 years	> 3 - ≤ 4 years	> 4 - ≤ 5 years	> 5 years	Total
Bonds	-	-	-	175,000	50,000	350,000	575,000
Mortgage bonds from central issuing institutions	246,000	84,000	183,000	120,000	121,000	1,288,000	2,042,000
<b>Total</b>	<b>246,000</b>	<b>84,000</b>	<b>183,000</b>	<b>295,000</b>	<b>171,000</b>	<b>1,638,000</b>	<b>2,617,000</b>

### 5.10.14 Presentation of value adjustments, provisions and reserves for general banking risks and changes therein during the current year

(CHF thousands)	Status 31.12.2016	2017					Status 31.12.2017
		Use in conformity with designated purpose	Currency differences	Past due interest, and recoveries	New creations charged to income	Releases to income	
<b>Provisions</b>							
Provisions for default risks	277	-10	-	-	24	-252	39
Provisions for other business risks	491	-32	-	-	-	-	459
Additional pension provision	2,400	-783	-	-	485	-	2,102
Provisions for deferred taxes	900	-	-	-	-	-	900
Other provisions	157	-	-	-	100	-157	100
<b>Total provisions</b>	<b>4,225</b>	<b>-825</b>	<b>-</b>	<b>-</b>	<b>609</b>	<b>-409</b>	<b>3,600</b>
<b>Reserves for general banking risks</b>	<b>411,886</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>26,114</b>	<b>-</b>	<b>438,000</b>
<b>Value adjustments for default and country risks</b>	<b>55,271</b>	<b>-836</b>	<b>-167</b>	<b>-</b>	<b>20,580</b>	<b>-12,749</b>	<b>62,099</b>
of which value adjustments for default risk from impaired loans	55,271	-836	-167	-	20,580	-12,749	62,099
of which value adjustments for latent risks	-	-	-	-	-	-	-

### 5.10.15 Disclosure of amounts due from / to related parties

(CHF thousands)	31.12.2017		31.12.2016	
	Amounts due from	Amounts due to	Amounts due from	Amounts due to
Holders of qualified participations	12,000	181,913	12,000	227,514
Group companies	-	78	2	173
Linked companies	10,316	123,960	10,300	153,618
Transactions with members of governing bodies	109,786	7,761	93,827	7,439

The above figures also include any off-balance sheet operation that may have been effected.

Loans to companies or entities related to the Canton consist of operating and investment loans granted on the basis of standard lending parameters.

Receivables from and payables to companies or entities related to the Canton are concluded at market conditions.

Loans to governing bodies primarily consist of mortgage loans and are granted at market conditions in compliance with standard lending parameters.

### 5.10.16 Presentation of the maturity structure of financial instruments

(CHF thousands)	At sight	Cancellable	Due				No maturity	Total
			within 3 months	within 3 to 12 months	within 1 to 5 years	after 5 years		
<b>Assets / Financial instruments</b>								
Liquid assets	2,036,626	-	-	-	-	-	-	2,036,626
Amounts due from banks	262,761	-	-	-	-	-	-	262,761
Amounts due from customers	13,495	471,923	398,184	183,475	501,762	306,392	-	1,875,231
Mortgage loans	5,258	169,229	762,303	969,348	4,156,926	2,769,748	-	8,832,812
Trading portfolio	40,833	-	-	-	-	-	-	40,833
Positive replacement values of derivative financial instruments	51,607	-	-	-	-	-	-	51,607
Financial investments	27,183	-	13,224	1,260	137,189	115,194	1,363	295,413
<b>Total</b>	<b>2,437,763</b>	<b>641,152</b>	<b>1,173,711</b>	<b>1,154,083</b>	<b>4,795,877</b>	<b>3,191,334</b>	<b>1,363</b>	<b>13,395,283</b>
Previous year	2,601,330	685,288	1,180,792	1,033,149	4,501,079	2,917,983	1,450	12,921,071
<b>Debt capital / Financial instruments</b>								
Amounts due to banks	168,482	20,037	295,010	4,000	30,000	-	-	517,529
Liabilities from securities financing transactions	-	-	70,000	-	-	-	-	70,000
Amounts due in respect of customer deposits	4,928,831	3,360,111	393,822	40,008	276,547	103,232	-	9,102,551
Negative replacement values of derivative financial instruments	28,663	-	-	-	-	-	-	28,663
Cash bonds	-	-	307	62	736	-	-	1,105
Bond issues and central mortgage institution loans	-	-	104,000	142,000	733,000	1,638,000	-	2,617,000
<b>Total</b>	<b>5,125,976</b>	<b>3,380,148</b>	<b>863,139</b>	<b>186,070</b>	<b>1,040,283</b>	<b>1,741,232</b>	<b>-</b>	<b>12,336,848</b>
Previous year	5,521,288	3,105,668	667,762	431,922	1,188,485	1,426,860	-	12,341,985

### 5.10.17 Presentation of assets and liabilities by domestic and foreign origin (domicile principle)

(CHF thousands)	31.12.2017		31.12.2016	
	Switzerland	Foreign	Switzerland	Foreign
<b>Assets</b>				
Liquid assets	2,036,557	69	2,204,578	189
Amounts due from banks	109,317	153,444	193,997	101,739
Amounts due from customers	1,578,904	296,327	1,564,618	280,800
Mortgage loans	8,832,812	-	8,227,790	-
Trading portfolio assets	21,776	19,057	16,294	11,499
Positive replacement values of derivative financial instruments	44,358	7,249	19,606	4,463
Financial investments	171,314	124,099	160,032	135,466
Accrued income and prepaid expenses	11,312	690	12,586	864
Non-consolidated participations	6,234	295	5,629	760
Tangible fixed assets	80,111	-	82,400	-
Intangible assets	14,302	-	21,364	-
Other assets	17,774	-	278,673	-
<b>Total assets</b>	<b>12,924,771</b>	<b>601,230</b>	<b>12,787,567</b>	<b>535,780</b>
<b>Liabilities</b>				
Amounts due to banks	289,323	228,206	638,736	217,548
Liabilities from securities financing transactions	70,000	-	125,000	-
Amounts due in respect of customer deposits	6,743,248	2,359,303	6,350,356	2,411,868
Negative replacement values of derivative financial instruments	25,021	3,642	47,741	4,549
Cash bonds	1,105	-	3,187	-
Bond issues and central mortgage institution loans	2,617,000	-	2,543,000	-
Accrued expenses and deferred income	41,750	262	43,044	34
Other liabilities	125,935	-	11,783	-
Provisions	3,600	-	4,225	-
Reserves for general banking risks	438,000	-	411,886	-
Endowment capital	300,000	-	240,000	-
Statutory retained earnings reserve	234,772	-	225,324	-
Group profit	44,834	-	45,066	-
<b>Total liabilities</b>	<b>10,934,588</b>	<b>2,591,413</b>	<b>10,689,348</b>	<b>2,633,999</b>

The breakdown by domestic and foreign origin is made on the basis of the customer's domicile, with the exception of mortgage loans where the domicile of the property is the relevant criterion. Liechtenstein is deemed to be a foreign country.

### 5.10.18 Breakdown of total assets by country or group of countries (domicile principle)

(CHF thousands)	31.12.2017		31.12.2016	
	Absolute	Share as %	Absolute	Share as %
<b>Assets domiciled abroad</b>				
<b>Europe</b>	<b>337,418</b>	<b>2.49</b>	<b>386,629</b>	<b>2.90</b>
Bulgaria	-		11,075	
Croatia	3,401		10,095	
France	29,827		26,775	
Germany	13,318		68,068	
Italy	105,121		89,132	
Liechtenstein	15,713		9,700	
Luxembourg	64,396		68,383	
Malta	19,519		-	
Norway	10		6,551	
Netherlands	10,767		6,559	
United Kingdom	51,890		36,126	
Sweden	-		10,278	
Other countries	23,456		43,887	
<b>North America</b>	<b>146,996</b>	<b>1.09</b>	<b>33,423</b>	<b>0.25</b>
United States	140,964		27,970	
Other countries	6,032		5,453	
<b>Asia</b>	<b>83,620</b>	<b>0.61</b>	<b>81,775</b>	<b>0.61</b>
Kazakhstan	68,340		66,912	
Singapore	4,893		5,099	
Other countries	10,387		9,764	
<b>Caribbean</b>	<b>20,185</b>	<b>0.15</b>	<b>26,584</b>	<b>0.20</b>
Panama	15,157		21,257	
Other countries	5,028		5,327	
<b>South America</b>	<b>7,587</b>	<b>0.06</b>	<b>5,233</b>	<b>0.04</b>
Mexico	5,866		5,177	
Other countries	1,721		56	
<b>Oceania</b>	<b>5,312</b>	<b>0.04</b>	<b>187</b>	<b>0.00</b>
<b>Other countries</b>	<b>112</b>	<b>-</b>	<b>1,949</b>	<b>0.01</b>
<b>Total assets abroad</b>	<b>601,230</b>	<b>4.44</b>	<b>535,780</b>	<b>4.02</b>
Switzerland	12,924,771	95.56	12,787,567	95.98
<b>Total assets</b>	<b>13,526,001</b>	<b>100.00</b>	<b>13,323,347</b>	<b>100.00</b>



#### 5.10.19 Breakdown of total assets by credit rating of country groups (risk domicile view)

Bank's own country rating (CHF thousands)	Standard & Poor's Rating	31.12.2017		31.12.2016	
		Net foreign exposure	Share as %	Net foreign exposure	Share as %
1 Excellent and high quality	AAA to AA-	355,822	59.2%	291,218	54.4%
2 Above-average quality	A+ to A-	22,763	3.8%	18,174	3.4%
3 Average quality	BBB+ to BBB-	193,791	32.2%	197,311	36.9%
4 Risk of default	BB+ to BB	9,035	1.5%	17,222	3.2%
5 Significant risk of default	BB-	2,083	0.3%	746	0.1%
6 Speculative, high risk of default	B+ to B-	435	0.1%	782	0.1%
7 Poor quality, very high risk	CCC+ to D	8	0.0%	465	0.1%
Unrated	-	17,293	2.9%	9,862	1.8%
<b>Total assets</b>		<b>601,230</b>	<b>100.0%</b>	<b>535,780</b>	<b>100.0%</b>

The breakdown by domestic and foreign origin is made on the basis of the customer's domicile, with the exception of mortgage loans where the domicile of the property is the relevant criterion. Liechtenstein is deemed to be a foreign country. Standard & Poor's ratings have been used since the beginning of 2017. The values of the previous year have been reclassified to ensure comparability.

## 5.10.20 Presentation of assets and liabilities broken down by the most significant currencies for the Bank

(CHF thousands)	Currencies				Total
	CHF	EUR	USD	Other	
<b>Assets</b>					
Liquid assets	1,964,391	67,971	2,275	1,989	2,036,626
Amounts due from banks	5,725	33,097	145,396	78,543	262,761
Amounts due from customers	1,359,271	314,006	189,920	12,034	1,875,231
Mortgage loans	8,832,812	-	-	-	8,832,812
Trading portfolio assets	5,320	15,187	271	20,055	40,833
Positive replacement values of derivative financial instruments	50,365	290	936	16	51,607
Financial investments	203,085	22,694	69,508	126	295,413
Accrued income and prepaid expenses	11,243	179	573	7	12,002
Non-consolidated participations	6,233	296	-	-	6,529
Tangible fixed assets	80,111	-	-	-	80,111
Intangible assets	14,302	-	-	-	14,302
Other assets	17,528	240	4	2	17,774
<b>Total assets shown in balance sheet</b>	<b>12,550,386</b>	<b>453,960</b>	<b>408,883</b>	<b>112,772</b>	<b>13,526,001</b>
Delivery entitlements from spot exchange, forward forex and forex options transactions <sup>1</sup>	80,728	1,672,578	888,296	192,579	2,834,181
<b>Total assets</b>	<b>12,631,114</b>	<b>2,126,538</b>	<b>1,297,179</b>	<b>305,351</b>	<b>16,360,182</b>
<b>Liabilities</b>					
Amounts due to banks	169,361	172,225	131,810	44,133	517,529
Liabilities from securities financing transactions	70,000	-	-	-	70,000
Amounts due in respect of customer deposits	6,365,207	1,640,168	903,426	193,750	9,102,551
Negative replacement values of derivative financial instruments	27,419	290	937	17	28,663
Cash bonds	1,105	-	-	-	1,105
Bond issues and central mortgage institution loans	2,617,000	-	-	-	2,617,000
Accrued expenses and deferred income	41,576	-	410	26	42,012
Other liabilities	125,512	246	68	109	125,935
Provisions	3,600	-	-	-	3,600
Reserves for general banking risks	438,000	-	-	-	438,000
Endowment capital	300,000	-	-	-	300,000
Statutory retained earnings reserve	234,772	-	-	-	234,772
Group's profit	44,834	-	-	-	44,834
<b>Total liabilities in balance sheet</b>	<b>10,438,386</b>	<b>1,812,929</b>	<b>1,036,651</b>	<b>238,035</b>	<b>13,526,001</b>
Delivery obligations from spot exchange, forward forex and forex options transactions <sup>1</sup>	2,156,449	314,678	259,871	66,895	2,797,893
<b>Total liabilities</b>	<b>12,594,835</b>	<b>2,127,607</b>	<b>1,296,522</b>	<b>304,930</b>	<b>16,323,894</b>
<b>Net position per currency</b>	<b>36,279</b>	<b>-1,069</b>	<b>657</b>	<b>421</b>	<b>36,288</b>
Net position per currency in the previous year	-13,674	726	-1,320	1,321	-12,947

<sup>1</sup> Options have been delta-weighted.



## 5.11 INFORMATION ON OFF-BALANCE SHEET TRANSACTIONS

### 5.11.21 Breakdown of contingent liabilities and contingent assets

(CHF thousands)	31.12.2017	31.12.2016
<b>Contingent liabilities</b>		
Guarantees to secure credit and similar	74,505	67,337
Performance guarantees and similar	28,787	26,605
Irrevocable commitments arising from documentary letters of credit	36,789	51,356
<b>Total contingent liabilities</b>	<b>140,081</b>	<b>145,298</b>

### 5.11.22 Breakdown of fiduciary transactions

(CHF thousands)	31.12.2017	31.12.2016
Fiduciary investments	183,624	99,855
Fiduciary loans	8,334	6,653
<b>Total fiduciary transactions</b>	<b>191,958</b>	<b>106,508</b>

## 5.12 INFORMATION ON THE INCOME STATEMENT

### 5.12.23 Breakdown of the result from trading activities and fair value option

(CHF thousands)	2017	2016
Result from trading activities from:		
Foreign currencies	9,998	14,762
Banknote trading	6,567	769
Commodities / precious metals	1,292	1,377
Securities trading	434	-117
<b>Total result from trading activities</b>	<b>18,291</b>	<b>16,791</b>

### 5.12.24 Disclosure of material refinancing income in the item Interest and discount income as well as material negative interest

Refinancing income in the item "Result from interest operations"		
Interest and dividend income from trading portfolio is offset with costs of refinancing of that portfolio.		
(CHF thousands)	2017	2016
<b>Negative interest</b>		
Negative interest on assets (decrease in interest and discount income)	4,718	5,049
Negative interest on commitments (decrease in interest expenses)	3,242	3,178

### 5.12.25 Breakdown of personnel expenses

(CHF thousands)	2017	2016
Salaries	65,857	63,452
<i>of which expenses relating to share-based compensation and alternative forms of variable compensation</i>	-	-
Social benefits	15,203	13,222
Other personnel expenses	2,874	2,742
<b>Total personnel expenses</b>	<b>83,934</b>	<b>79,416</b>

### 5.12.26 Breakdown of other operating expenses

(CHF thousands)	2017	2016
Office space expenses	5,500	6,203
Expenses for information and communications technology	20,378	17,046
Expenses for vehicles, equipment, furniture and other fixtures as well as operating lease expenses	426	350
Fees of audit firm	834	805
<i>of which for financial and regulatory audits</i>	792	710
<i>of which for other services</i>	42	95
Other operating expenses	11,633	12,659
<i>of which compensation for any State guarantee</i>	-	-
<b>Total other operating expenses</b>	<b>38,771</b>	<b>37,063</b>

## 5.12.27 Explanations regarding material losses, extraordinary income and expenses, material releases of hidden reserves, reserves for general banking risks, and value adjustments and provisions no longer required

<p><b>5.12.27.1 Material losses</b> No material losses were incurred during the financial year.</p>
<p><b>5.12.27.2 Extraordinary income and extraordinary expenses</b> The extraordinary amount of CHF 2.5 million is mainly due to the proceeds from the variable portion of the sales price of our participation in Swisscanto Holding AG which was concluded in 2015.</p>
<p><b>5.12.27.3 Hidden reserves</b> The Group does not hold any hidden reserve, and discloses its financial statements on the basis of the true and fair view principle.</p>
<p><b>5.12.27.4 Reserves for general banking risks</b> CHF 26.1 million were deducted from "Changes in reserves for general banking risks" to create reserves for general banking risks.</p>
<p><b>5.12.27.5 Value adjustments and provisions no longer required</b> There is no relevant information to provide under this heading.</p>
<p><b>5.12.27.6 Revaluations of participations and tangible fixed assets</b> There were no revaluations of participations or tangible fixed assets during the financial year.</p>

## 5.12.28 Presentation of current and deferred taxes, and disclosure of tax rate

(CHF thousands)	31.12.2017	31.12.2016
Current taxes	710	606
Real estate tax	317	266
Provisions for deferred taxes	-	-
<b>Total taxes</b>	<b>1,027</b>	<b>872</b>
<b>Average tax rate weighted on the basis of the operating result<sup>1</sup></b>	<b>1.0%</b>	<b>0.9%</b>

<sup>1</sup> The Parent company Banca dello Stato del Cantone Ticino is exempt from federal, cantonal and communal taxation. It is subject to real estate taxation.



## **Report of the auditor** **to the Council and to the Cantonal Parliament of the Republic** **and Canton of Ticino, Bellinzona**

### **Report on the audit of the consolidated financial statements**

#### **Opinion**

We have audited the consolidated financial statements of the Group Banca dello Stato del Cantone Ticino and its subsidiaries ("the Group"), which comprise the consolidated balance sheet as at 31 December 2017, consolidated income statement, consolidated cash flow statement, consolidated statement of changes in equity and notes for the year then ended, including a summary of significant accounting policies (pages 36-66).

In our opinion, the consolidated financial statements as at 31 December 2017 give a true and fair view of the financial position, the results of operations and the cash flow in accordance with accounting rules for banks and comply with Swiss law and the Law on Banca dello Stato del Cantone Ticino.

#### **Basis for opinion**

We conducted our audit in accordance with Swiss law and Swiss Auditing Standards. Our responsibilities under those provisions and standards are further described in the "Auditor's responsibilities for the audit of the consolidated financial statements" section of our report.

We are independent of the Group in accordance with the provisions of Swiss law and the requirements of the Swiss audit profession and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **Our audit approach**

##### **Overview**



- Overall group materiality: CHF 3.5 million
- We performed full scope audits at Banca dello Stato del Cantone Ticino and Axion Swiss Bank SA.

Taken together, our audit work covers 100% of the operating result of the Group.

As key audit matter the following area of focus has been identified:

- Impairment of amounts due from customers and mortgage loans

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### ***Audit scope***

We designed our audit by determining materiality and assessing the risks of material misstatement in the consolidated financial statements. In particular, we considered where subjective judgements were made; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

### ***Materiality***

The scope of our audit was influenced by our application of materiality. Our audit opinion aims to provide reasonable assurance that the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall group materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the consolidated financial statements as a whole.

<b><i>Overall group materiality</i></b>	CHF 3.5 million
<b><i>How we determined it</i></b>	5% of the operating result (result of the period before tax, changes in reserves for general banking risks and extraordinary items).
<b><i>Rationale for the materiality benchmark applied</i></b>	We chose the operating result (result of the period before tax, changes in reserves for general banking risks and extraordinary items) because it is the benchmark against which the performance of a banking group is most commonly measured and it is the generally accepted benchmark in the financial industry.

We agreed with the Audit Committee of the Board of Directors that we would report to them misstatements above CHF 173'500 identified during our audit as well as any misstatements below that amount which, in our view, warranted reporting for qualitative reasons.

### ***Report on key audit matters based on the circular 1/2015 of the Federal Audit Oversight Authority***

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



## Impairment of amounts due from customers and mortgage loans

<i>Key audit matter</i>	<i>How our audit addressed the key audit matter</i>
<p>As shown in the note 5.10.2 of the annual report 2017, the Group grants loans and advances to customers and mortgage loans (79% of total assets or CHF 10'708 million). We consider the valuation of amounts due from clients and mortgage loans that show signs of potential default to be a key audit matter on the basis of the significance of the related balance sheet positions. Moreover, the determination of the amount of any write-down is based on the debtor's capacity to repay the amount due and/or the liquidation value of the collateral, both of which may be influenced by subjective factors.</p> <p>The Group has a control system in place that enables its various governing bodies to identify and to analyze the risk of default, to take precautionary measures and to calculate the necessary impairment charges.</p> <p>The accounting and valuation principles for amounts due from clients and the methods used to identify default risks and determine the need for impairment are described in the notes to the consolidated financial statements (sections 5.2.3.3, 5.4.1 and 5.5).</p>	<p>We checked and tested the key controls relating to credit transactions:</p> <ul style="list-style-type: none"><li>• controls aimed to identify signs of potential default in order to determine the scope of non-performing and/or impaired loans;</li><li>• controls relating to the calculation of value adjustment including the determination of the market value of the collaterals.</li></ul> <p>In addition, we checked on a sample basis that:</p> <ul style="list-style-type: none"><li>• the risk category given to the selected credit was adequate;</li><li>• the market value of the collateral was determined or updated in accordance with market practice;</li><li>• the value adjustments and provisions were calculated and recorded in accordance with the accounting principles.</li></ul> <p>On the basis of our audit procedures, we consider the valuation of amounts due from clients and mortgage loans to be adequate.</p>

## Responsibilities of the Board of Directors for the consolidated financial statements

The Board of Directors is responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with accounting rules for banks, the provisions of Swiss law and the Law on Banca dello Stato del Cantone Ticino, and for such internal control as the Board of Directors determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

## Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's 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 Swiss law and Swiss Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.



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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control;
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made;
- Conclude on the appropriateness of the Board of Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern;
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the Board of Directors or its relevant committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Board of Directors or its relevant committee with a statement that we have complied with relevant ethical requirements regarding independence, and to 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 the Board of Directors or its relevant committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's 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 on other legal and regulatory requirements***

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system exists which has been designed for the preparation of consolidated financial statements according to the instructions of the Board of Directors.

We recommend that the consolidated financial statements submitted to you be approved.

PricewaterhouseCoopers Ltd

A handwritten signature in blue ink, appearing to read 'Glenda Brändli', with a stylized flourish at the end.

Glenda Brändli  
Audit expert  
Auditor in charge

A handwritten signature in blue ink, appearing to read 'Lorenzo Morelli', with a stylized flourish at the end.

Lorenzo Morelli  
Audit expert

Lugano, 27 March 2018

# I. Information on Capital Adequacy Basel III and on Liquidity (unaudited data)

## I.I ADDITIONAL INFORMATION ON RISKS AND CAPITAL ADEQUACY (BASEL III)

For the calculation of capital adequacy requirements, the Group applies the following approaches:

- **Credit Risks:**

Basis: international approach (SA-BIS)

Value adjustments and provisions: exposures are risk-weighted net of specific provisions

Derivatives: current exposure method

Collateralised transactions: comprehensive approach

External credit assessment: external credit assessment was not used; FiRE for some types of exposures, use of SERV ratings

Netting: the net exposure of loans with respect to a counterparty did not take into account any netting agreements

- **Market Risks:**

Basis: standardised approach for market risks

Derivatives: delta-plus approach

General market risk on changes in market interest rates within the trading portfolio: maturity method

- **Operational Risks:**

Basis: basic indicator approach (BIA)

Qualitative information required by the Ordinance on Capital Adequacy can be found in Section 5.4 Risk Management of the Notes to the Group Financial Statements.

The information on risk and capital in the following tables is based on rules and approaches defined in Basel III. This information may differ from that presented in the previous tables due to these specific calculation rules.

## I.II PRESENTATION OF RECOGNISED REGULATORY CAPITAL

(CHF thousands)	31.12.2017	31.12.2016	Notes
Endowment capital	300,000	240,000	I.IV
Statutory retained earnings reserves	243,478	235,955	I.IV
Reserves for general banking risks	438,000	411,886	I.IV
<b>Total common equity Tier 1 capital</b>	<b>981,478</b>	<b>887,841</b>	
Other elements to be deducted from common equity capital	-14,302	-21,364	I.IV
<b>Total net common equity Tier 1 capital (net CET1)</b>	<b>967,176</b>	<b>866,477</b>	
Additional Tier 1 capital (AT1)	80,000	140,000	I.IV
<b>Total net Tier 1</b>	<b>1,047,176</b>	<b>1,006,477</b>	
Tier 2 capital (T2)	87,500	105,000	I.IV
<b>Total recognized regulatory capital</b>	<b>1,134,676</b>	<b>1,111,477</b>	
<b>Total risk-weighted positions</b>	<b>6,629,602</b>	<b>6,420,199</b>	

The BancaStato Group (Parent Bank) consolidated financial statements include Axion Swiss Bank SA Lugano. The Parent Bank holds 100% ownership. There are no differences between the scope of consolidation for accounting purposes and the scope of consolidation pertaining to the calculation of capital.

### I.III REQUIRED CAPITAL

(CHF thousands)	<b>31.12.2017</b>	<b>31.12.2016</b>
Credit risk	489,855	474,316
Risks not related to counterparties	6,557	6,747
Market risks	2,975	2,467
Operating risks	30,910	29,575
Other capital requirements	71	510
<b>Required capital</b>	<b>530,368</b>	<b>513,615</b>

### I.IV RATIOS

(as a % of risk-weighted positions)	<b>31.12.2017</b>
Net CET1 ratio	14.6%
Net Tier 1 ratio	15.8%
Total regulatory capital ratio	17.1%
CET1 requirements under the terms of CAO transitional provisions	6.5%
<i>of which capital buffer</i>	1.3%
<i>of which countercyclical capital buffer (% of risk-weighted positions)</i>	0.8%
CET1 available for the coverage of minimum requirements and buffers, after deduction of AT1 and T2 requirements covered by CET1	13.6%
CET1 target based on FINMA Circular 11/2 "Capital buffer and capital planning" plus countercyclical capital buffer	8.2%
Available CET1	13.3%
T1 target based on FINMA 11/2 plus countercyclical buffer	9.8%
Available T1	14.9%
Regulatory capital target based on FINMA Circular 11/2 plus countercyclical buffer	12.0%
Available regulatory capital	17.1%

### I.V ASSETS' CREDIT QUALITY

(CHF thousands)	Gross book value		Value adjustments	Net amounts
	Default positions	Non-default positions		
Receivables	161,097	10,871,806	-62,099	10,970,804
Debt instruments	-	259,478	-	259,478
Off-balance sheet exposures	39	203,835	-39	203,835
<b>Total</b>	<b>161,136</b>	<b>11,335,119</b>	<b>-62,138</b>	<b>11,434,117</b>
Off-balance sheet exposures	142,669	10,772,002	-55,548	10,859,123

Default positions are those positions for which it is unlikely that the debtors will be able to fulfill their future obligations or for which the payment of interest, commissions and amortisation (in part or in full) is over 90 days overdue. All default positions are assessed individually. A value adjustment is made for the uncollateralised portion valued at its liquidation value, and taking into account the debtor's credit rating.

## I.VI CHANGES IN THE LOAN PORTFOLIO AND DEBT INSTRUMENTS IN DEFAULT

(CHF thousands)	2017	2016
Loans and debt instruments in default at the beginning of the year	140,847	175,898
Loans and debt instruments that defaulted in the year under review	70,903	25,808
Positions no longer in default	-52,032	-48,028
Amortised amounts	-836	-2,237
Other changes	2,215	-10,594
<b>Total loans and debt instruments in default at year-end</b>	<b>161,097</b>	<b>140,847</b>

The item "Other changes" consists primarily of balance variations in open positions.

## I.VII ADDITIONAL INFORMATION ON ASSET CREDIT QUALITY

Default loans are those credits for which it is unlikely that the debtors will be able to fulfill their future obligations or for which the payment of interest, commissions and amortisation (in part or in full) is over 90 days overdue.

All default loans are assessed individually. A value adjustment is made for the uncollateralised portion valued at its liquidation value, taking into account the debtor's credit rating.

### I.VII.I Credit risk by economic activity

(CHF thousands)	2017	2016
<b>Gross amount of defaulted loans</b>		
<b>Economic activity</b>		
Agriculture	1,020	22
Non-financial private companies	1,761	1,809
Banks and securities dealers	50	217
Households	87,023	90,791
Industry	40,301	36,795
Non-commercial private institutions	363	445
Service companies	30,555	10,640
Public sector	24	128
<b>Current year total</b>	<b>161,097</b>	<b>140,847</b>

### I.VII.II Credit risk broken down by residual duration

(CHF thousands)	At sight / cancellable	Due				No maturity	Total
		within 3 months	within 3 to 12 months	within 1 to 5 years	over 5 years		
Agriculture	1,020	-	-	-	-	-	1,020
Non-financial private companies	1,761	-	-	-	-	-	1,761
Banks and securities dealers	50	-	-	-	-	-	50
Households	41,421	4,955	6,167	33,493	987	-	87,023
Industry	30,659	5,042	1,725	2,875	-	-	40,301
Non-commercial private institutions	363	-	-	-	-	-	363
Service companies	11,290	4,178	2,263	12,824	-	-	30,555
Public sector	24	-	-	-	-	-	24
<b>Current year total</b>	<b>86,588</b>	<b>14,175</b>	<b>10,155</b>	<b>49,192</b>	<b>987</b>	<b>-</b>	<b>161,097</b>

### I.VIII CREDIT RISK MITIGATION AT 31.12.2017

(CHF thousands)	Positions with other collateral	Positions with financial collateral or credit derivatives	Uncollateralised positions	Total
Loans (including debt instruments)	8,301,218	550,336	2,378,728	11,230,282
Off-balance sheet transactions	6,372	36,425	161,038	203,835
<b>Total</b>	<b>8,307,590</b>	<b>586,761</b>	<b>2,539,766</b>	<b>11,434,117</b>
<i>of which in default</i>	<i>86,734</i>	<i>2,478</i>	<i>11,192</i>	<i>100,404</i>
Total previous year	7,823,131	592,255	2,443,737	10,859,123
<i>of which in default</i>	<i>79,918</i>	<i>984</i>	<i>11,543</i>	<i>92,445</i>

### I.IX BREAKDOWN OF CREDIT RISK AT 31.12.2017

(CHF thousands)	Statutory risk-weighting								Total
	0%	20%	35%	50%	75%	100%	150%	≥ 250%	
<b>Exposures</b>									
Central governments and central banks	15,327	-	-	-	-	-	-	-	15,327
Banks and securities dealers	-	209,878	-	84,454	-	24	1	-	294,357
Public sector entities	17,069	188,213	801	709,965	-	17,404	23	-	933,475
Corporations	-	136,061	18,731	15	929	612,359	2,773	-	770,868
Retail	-	-	6,037,160	-	744,560	2,205,410	19,288	-	9,006,418
Equity-type securities	-	-	-	-	-	22,167	20,435	-	42,602
Other exposures	2,036,626	-	-	-	-	126	-	-	2,036,752
<b>Total</b>	<b>2,069,022</b>	<b>534,152</b>	<b>6,056,692</b>	<b>794,434</b>	<b>745,489</b>	<b>2,857,490</b>	<b>42,520</b>	<b>-</b>	<b>13,099,799</b>
<i>of which covered by mortgage</i>	-	-	<i>6,056,692</i>	-	<i>229,002</i>	<i>1,896,503</i>	-	-	<i>8,182,197</i>
<i>of which past-due loans</i>	-	-	-	-	-	<i>41,158</i>	<i>22,086</i>	-	<i>63,244</i>

## I.X LEVERAGE RATIO AND CALCULATION OF GLOBAL EXPOSURE SUBJECT TO LEVERAGE RATIO

(CHF thousands)		31.12.2017	31.12.2016
<b>1</b>	<b>Global exposure subject to ratio leverage effect (vs. assets in balance sheet)</b>	<b>13,868,158</b>	<b>13,761,939</b>
+	Total assets as per disclosed Annual Report	13,526,001	13,323,347
-	Adjustment of assets deducted from Tier 1 capital and relating to entities not included in the regulatory consolidation scope	-14,302	-21,364
+	Adjustments on derivative financial instruments	37,149	34,260
+	Adjustments relating to securities financing transactions	1,504	124,622
+	Adjustments relating to off-balance sheet transactions	317,806	301,074
<b>2</b>	<b>Global exposure subject to leverage effect ratio</b>	<b>13,868,158</b>	<b>13,761,939</b>
<b>2.1</b>	<b>Balance sheet exposure</b>	<b>13,460,092</b>	<b>13,277,914</b>
+	Balance sheet exposures excluding derivatives and securities financing transactions	13,474,394	13,299,278
-	Assets deducted from considered Tier 1 capital	-14,302	-21,364
<b>2.2</b>	<b>Derivative exposure</b>	<b>88,756</b>	<b>58,329</b>
+	Positive replacement value of all derivative transactions taking into account margin payments	51,607	24,069
+	Add-ons in relation to all derivatives	37,149	34,260
<b>2.3</b>	<b>Exposure relating to securities financing transactions</b>	<b>1,504</b>	<b>124,622</b>
<b>2.4</b>	<b>Other off-balance sheet exposures</b>	<b>317,806</b>	<b>301,074</b>
+	Off-balance sheet exposure at gross nominal value before credit conversion factor	1,917,055	1,935,913
-	Adjustment after credit conversion factor	-1,599,249	-1,634,839
<b>3</b>	<b>Net Tier 1 capital</b>	<b>1,047,176</b>	<b>1,006,477</b>
<b>4</b>	<b>Basel III leverage ratio</b>	<b>7.6%</b>	<b>7.3%</b>

## I.XI INFORMATION ON LIQUIDITY COVERAGE RATIO (LCR)

(CHF thousands)	Q1 2017 <sup>1</sup>	Q2 2017 <sup>1</sup>	Q3 2017 <sup>1</sup>	Q4 2017 <sup>1</sup>
High quality liquid assets (HQLA) <sup>2</sup>	1,928,171	1,857,731	1,980,145	2,053,235
of which level 1 assets	1,806,238	1,747,419	1,865,140	1,934,381
of which level 2 assets	121,933	110,312	115,005	118,854
Net outflows	1,129,651	1,279,527	1,297,807	1,110,518
<b>Short-term liquidity coverage ratio (LCR)</b>	<b>171%</b>	<b>145%</b>	<b>153%</b>	<b>185%</b>
Previous year	130%	195%	214%	212%

<sup>1</sup> Average for the quarter, calculated on the basis of monthly statistics.

<sup>2</sup> In accordance with FINMA regulatory requirements, refer to Circular 2015/2 "Liquidity Risks - banks"

# Individual Financial Statements

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# 1. Balance Sheet

(CHF thousands)	Notes	31.12.2017	31.12.2016	Change
<b>Assets</b>				
Liquid assets		1,328,273	1,294,087	34,186
Amounts due from banks		299,948	278,604	21,344
Amounts due from customers	5.6.2	1,595,118	1,584,040	11,078
Mortgage loans	5.6.2	8,832,812	8,227,790	605,022
Trading portfolio	5.6.3	33,889	24,580	9,309
Positive replacement values of derivative financial instruments	5.6.4	54,679	24,353	30,326
Financial investments	5.6.5	288,487	290,954	-2,467
Accrued income and prepaid expenses		11,885	13,319	-1,434
Participations		72,668	80,068	-7,400
Tangible fixed assets		78,051	79,190	-1,139
Other assets	5.6.6	17,312	276,010	-258,698
<b>Total assets</b>		<b>12,613,122</b>	<b>12,172,995</b>	<b>440,127</b>
Total subordinated claims		40,929	42,964	-2,035
<i>of which subject to mandatory conversion and/or debt waiver</i>		40,929	42,495	-1,566
<b>Liabilities</b>				
Amounts due to banks		726,130	950,911	-224,781
Liabilities from securities financing transactions	5.6.1	70,000	125,000	-55,000
Amounts due in respect of customer deposits		7,980,856	7,525,083	455,773
Negative replacement values of derivative financial instruments	5.6.4	29,382	47,697	-18,315
Cash bonds		1,105	3,187	-2,082
Bond issues and central mortgage institution loans	5.6.7	2,617,000	2,543,000	74,000
Accrued expenses and deferred income		35,957	36,785	-828
Other liabilities	5.6.6	123,926	10,650	113,276
Provisions	5.6.9	2,600	3,325	-725
Reserves for general banking risks	5.6.9	438,000	411,886	26,114
Endowment capital	4 and 5.6.10	300,000	240,000	60,000
Statutory retained earnings reserve	4	240,028	228,307	11,721
Profit (result for the period)	4	48,138	47,164	974
<b>Total liabilities</b>		<b>12,613,122</b>	<b>12,172,995</b>	<b>440,127</b>
Total subordinated liabilities		255,273	315,273	-60,000
<i>of which subject to mandatory conversion and/or debt waiver</i>		80,000	140,000	-60,000
<b>Off-balance sheet transactions</b>				
Contingent liabilities	5.6.2	133,497	147,884	-14,387
Irrevocable commitments	5.6.2	36,845	56,943	-20,098
Obligations to pay up and make further contributions	5.6.2	14,180	14,180	-

## 2. Income Statement

(CHF thousands)	Notes	2017	2016	Change
<b>Income and expenses from ordinary banking activities</b>				
<b>Result from interest operations</b>				
Interest and discount income		178,862	178,712	150
Interest and dividend income from financial investments		2,657	3,480	-823
Interest expense		-45,173	-47,883	2,710
<b>Gross result from interest operations</b>		<b>136,346</b>	<b>134,309</b>	<b>2,037</b>
Changes in value adjustments for default risk and losses from interest operations		-7,290	-2,251	-5,039
<b>Net result from interest operations</b>		<b>129,056</b>	<b>132,058</b>	<b>-3,002</b>
<b>Result from commission business and services</b>				
Commission income from securities trading and investment activities		24,282	22,133	2,149
Commission income from lending activities		3,680	3,223	457
Commission income from other services		7,927	7,655	272
Commission expense		-6,839	-6,563	-276
<b>Result from trading activities and fair value option</b>	5.8.15	<b>14,726</b>	<b>13,306</b>	<b>1,420</b>
<b>Other results from ordinary activities</b>				
Result from the disposal of financial investments		1,289	294	995
Income from participations		2,873	2,200	673
Result from real estate		827	176	651
Other ordinary income		3,836	3,677	159
Other ordinary expenses		-168	-15	-153
<b>Net revenues</b>		<b>181,489</b>	<b>178,144</b>	<b>3,345</b>
<b>Operating expenses</b>				
Personnel expenses	5.8.17	-68,529	-64,906	-3,623
Other operating expenses	5.8.18	-33,359	-32,345	-1,014
<b>Value adjustments on participations and depreciation and amortisation of tangible fixed assets and intangible assets</b>		<b>-7,641</b>	<b>-11,496</b>	<b>3,855</b>
<b>Changes to provisions and other value adjustments, and losses</b>		<b>80</b>	<b>-385</b>	<b>465</b>
<b>Operating result</b>		<b>72,040</b>	<b>69,012</b>	<b>3,028</b>
<b>Extraordinary income</b>	5.8.19.02	<b>2,545</b>	<b>2,460</b>	<b>85</b>
<b>Extraordinary expenses</b>	5.8.19.02	<b>-16</b>	<b>-42</b>	<b>26</b>
<b>Changes in reserves for general banking risks</b>	5.8.19.04	<b>-26,114</b>	<b>-24,000</b>	<b>-2,114</b>
<b>Taxes</b>	5.8.20	<b>-317</b>	<b>-266</b>	<b>-51</b>
<b>Profit (result for the period)</b>		<b>48,138</b>	<b>47,164</b>	<b>974</b>

### 3. Proposed Appropriation of Retained Earnings

(CHF thousands)	2017	2016	Change
<b>Appropriation of retained earnings</b>			
Profit (result of the period)	48,138	47,164	974
Amount carried forward	-	-	-
<b>Balance sheet profit</b>	<b>48,138</b>	<b>47,164</b>	<b>974</b>
<b>Proposal of the Board of Directors</b>			
Assignment to the statutory retained earnings reserve	12,046	11,721	325
5% interest on the endowment capital	12,000	12,000	-
Additional payment to the Canton	24,092	23,443	649
<b>Amount carried forward</b>	<b>-</b>	<b>-</b>	<b>-</b>

## 4. Statement of Changes in Equity

(CHF thousands)	Endowment capital	Retained earnings reserve	Reserves for general banking risks	Result of the period	<b>Total</b>
<b>Equity at 1.1.2017</b>	240,000	228,307	411,886	47,164	927,357
<b>Appropriation of retained earnings 2016</b>					
<i>Assignment to the statutory retained earnings reserve</i>	-	+11,721	-	-11,721	-
<i>5% interest on the endowment capital</i>	-	-	-	-12,000	-12,000
<i>Additional payment to the Canton</i>	-	-	-	-23,443	-23,443
Endowment capital increase	+60,000	-	-	-	60,000
Allocation to reserves for general banking risks	-	-	+26,114	-	26,114
Profit (result for the period)	-	-	-	+48,138	48,138
<b>Total equity at 31.12.2017</b>	<b>300,000</b>	<b>240,028</b>	<b>438,000</b>	<b>48,138</b>	<b>1,026,166</b>

## 5. Notes to the Financial Statements

### 5.1 ACTIVITIES OF THE BANK AND PERSONNEL

#### 5.1.1 Activities of the Bank

Banca dello Stato del Cantone Ticino (BancaStato), based in Bellinzona, is an autonomous banking institution under public law which operates as a full service bank whose primary aim is to favour the development of the economy in Ticino.

Its operations have evolved over 100 years and comprise the complete range of banking services provided by full service banks. These activities are geared towards facilitating access to capital for small and medium-sized companies as well as individuals.

In 2010 and 2013, as part of a move to diversify its sources of revenue, BancaStato acquired the entire capital of AHSA Holding SA, Lugano, in order to gain indirect control over Axion Swiss Bank SA, Lugano (Axion). At end-2016, BancaStato acquired the entire capital of Axion from AHSA Holding SA. During 2017 the capital of AHSA Holding SA was entirely reimbursed, but the cancellation from the Commerce Registry of Canton Ticino is still pending.

Axion Swiss Bank SA's primary business focus is on portfolio management for private and institutional clients. The Bank is active on primary international markets. In the first quarter of 2016, within the framework of a strategy aimed at strengthening its asset administration business, Axion acquired a portion of client assets and infrastructure from Société Générale Private Banking (Lugano-Svizzera) SA.

With the aim of jointly creating a service platform for external asset managers, BancaStato acquired, in 2016, a minority share (30%) in Soave Asset Management Ltd., Lugano as well as a minority share (30%) in Londinium Dac, Dublin. Soave Asset Management Ltd. is active in asset management while Londinium Dac is authorized to operate as an investment company in accordance with the MiFID, providing onshore investment and savings management services.

#### 5.1.2 Personnel

As at 31 December 2017, the Bank had a total of 427 employees on payroll (388.05 FTEs) with apprentices calculated at 50%, compared to 432 staff at the end of 2016 (392.9 FTEs).

### 5.2 ACCOUNTING AND VALUATION PRINCIPLES

#### 5.2.1 General principles

The financial statements of Banca dello Stato del Cantone Ticino as at 31 December 2017 were prepared in accordance with applicable legal and regulatory provisions as well as the true and fair view principle, in compliance with the provisions of the Swiss Code of Obligations and the Swiss Banking legislation, in particular the guidelines of the Swiss Financial Market Supervisory Authority FINMA and the Swiss listing rules.

All business transactions are recorded at the time they are closed. The balance sheet is presented on a transactions date basis.

#### 5.2.2 Accounting and valuation principles for individual financial statements

The valuation rules for the individual financial statements reflect those of the consolidated financial statements (refer to Section 5.2.2 and following of the Notes to the Group Financial Statements) except for the item below:

#### 5.2.3 Participations

Participations comprise company equity stakes held by the Bank as long-term investments.

Participations are carried at cost less appropriate depreciation, regardless of the share held.

This item also includes the goodwill of participations on which the Bank may exercise substantial influence.

#### 5.2.4 Commission expense

Commission expense for the year under review comprises outsourced services connected to payment transactions, securities administration and stock exchange/forex/treasury back-office for a total of CHF 2,011,000 (2016: CHF 2,253,000).



### **5.3 FOREIGN CURRENCY TRANSLATION**

Assets and liabilities denominated in foreign currency are converted into Swiss francs at the rate of exchange as at the balance sheet closing date. Resulting gains or losses are disclosed in the income statement under "Result from trading operations and fair value option".

Proceeds and expenses are converted at the exchange rate applicable on the date the individual transactions are recorded.

Exchange rates applied at the close of the financial year for the major currencies were as follows:

EUR 1.1703 (2016: 1.0724)

USD 0.9747 (2016: 1.0158)

### **5.4 CHANGES IN FINANCIAL STATEMENTS AND PRESENTATION OF ACCOUNTS**

There were no changes in the accounting principles in 2017.

### **5.5 OTHER INFORMATION**

For information on "Risk management", "Methods used for identifying default risks and determining the need for value adjustments", "Valuation of collateral", "Business policy regarding the use of derivative financial instruments, including explanations on hedge accounting", "Material events after the balance sheet date" and "Premature resignation of the auditors", refer to the Group Financial Statements as these points are also applicable to BancaStato's Individual Financial Statements.



## 5.6 INFORMATION ON THE BALANCE SHEET

### 5.6.1 Breakdown of securities financing transactions (assets and liabilities)

(CHF thousands)	31.12.2017	31.12.2016
<b>Securities lending, securities borrowing and repurchase agreements</b>		
Book value of receivables from cash collateral delivered in connection with securities borrowing and reverse repurchase transactions <sup>1</sup>	-	-
Book value of obligations from cash collateral received in connection with securities lending and repurchase agreements <sup>1</sup>	70,000	125,000
Book value of securities lent in connection with securities lending or delivered as collateral in connection with securities borrowing as well as securities in own portfolio transferred in connection with repurchase agreements.	68,641	122,804
<i>of which with unrestricted right to resell or repledge</i>	68,641	122,804
Fair value of securities received and serving as collateral in connection with securities lending or securities borrowed in connection with securities borrowing as well as securities received in connection with reverse repurchase agreements with an unrestricted right to resell or repledge.	-	-
<i>of which repledged securities</i>	-	-
<i>of which resold securities</i>	-	-

<sup>1</sup> Before any netting agreement.

## 5.6.2 Presentation of collateral for loans / receivables and off-balance sheet transactions, as well as impaired loans / receivables at 31.12.2017

(CHF thousands)	Type of collateral			
	Secured by mortgage	Other collateral	Unsecured	Total
<b>Loans (before netting with value adjustments)</b>				
Amounts due from customers	170,968	204,480	573,636	949,084
Amounts due from public corporations	61	692	686,402 <sup>1</sup>	687,155
Mortgage loans	8,853,705 <sup>1</sup>			8,853,705
<i>Residential property</i>	6,560,497			6,560,497
<i>Office and business premises</i>	1,135,964			1,135,964
<i>Commercial and industrial premises</i>	477,407			477,407
<i>Other</i>	679,837			679,837
<b>Total loans (before netting with value adjustments)</b>	<b>9,024,734</b>	<b>205,172</b>	<b>1,260,038</b>	<b>10,489,944</b>
Previous year	8,459,387	232,132	1,175,341	9,866,860
<b>Total loans (after netting with value adjustments)</b>	<b>9,003,841</b>	<b>198,372</b>	<b>1,225,717</b>	<b>10,427,930</b>
Previous year	8,434,588	225,252	1,151,990	9,811,830
<b>Off-balance sheet</b>				
Contingent liabilities	7,033	51,036	75,428	133,497
Irrevocable commitments	1,881	-	34,964 <sup>2</sup>	36,845
Obligations to pay up shares and make further contributions	-	-	14,180	14,180
<b>Total off-balance sheet</b>	<b>8,914</b>	<b>51,036</b>	<b>124,572</b>	<b>184,522</b>
Previous year	29,608	61,550	127,849	219,007

(CHF thousands)	Gross debt amount	Estimated liquidation value	Net debt amount	Individual value adjustments
<b>Impaired loans</b>				
<b>Current year</b>	<b>156,149</b>	<b>94,135</b>	<b>62,014</b>	<b>62,014</b>
<i>of which secured against collateral</i>	119,790	92,097	27,693	27,693
<i>of which unsecured</i>	36,359	2,038	34,321	34,321
Previous year	129,023	73,993	55,030	55,030
<i>of which secured against collateral</i>	102,349	70,671	31,678	31,678
<i>of which unsecured</i>	26,674	3,322	23,352	23,352

<sup>1</sup> Including loans to entities related to public institutions for CHF 136.4 million (2016: CHF 134.9 million).

<sup>2</sup> Including CHF 35 million (2016: CHF 34.1 million) as a required share for deposit guarantee purposes.

### 5.6.3 Breakdown of trading portfolios and fair value option

(CHF thousands)	31.12.2017	31.12.2016
<b>Trading portfolio (assets)</b>		
Equity-type securities	121	363
Shares in investment funds	13,713	9,139
Precious metals and commodities	20,055	15,078
<b>Total trading portfolio</b>	<b>33,889</b>	<b>24,580</b>
<i>of which determined using a valuation model</i>	-	-
<i>of which securities eligible for repo transactions in accordance with liquidity requirements</i>	-	-

### 5.6.4 Presentation of derivative financial instruments (assets and liabilities)

(CHF thousands)	Trading instruments			Hedging instruments		
	Replacement values		Contract volume	Replacement values		Contract volume
	positive	negative		positive	negative	
<b>Interest rate instruments</b>						
IRS	-	-	-	6,986	17,341	534,000
<b>Total interest rate instruments</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>6,986</b>	<b>17,341</b>	<b>534,000</b>
<b>Foreign currencies / precious metals</b>						
Forward contracts	730	451	81,596	-	101	26,348
Swaps (interest rate/currency)	3,659	3,680	452,848	42,012	6,517	2,653,649
Options (OTC)	1,292	1,292	185,809	-	-	-
<b>Total foreign currencies / precious metals</b>	<b>5,681</b>	<b>5,423</b>	<b>720,253</b>	<b>42,012</b>	<b>6,618</b>	<b>2,679,997</b>
<b>Total before netting agreements</b>	<b>5,681</b>	<b>5,423</b>	<b>720,253</b>	<b>48,998</b>	<b>23,959</b>	<b>3,213,997</b>
<i>of which determined using a valuation model</i>	<i>5,681</i>	<i>5,423</i>	<i>-</i>	<i>48,998</i>	<i>23,959</i>	<i>-</i>
Total previous year	2,524	2,332	362,685	21,829	45,365	3,652,001
<i>of which determined using a valuation model</i>	<i>2,524</i>	<i>2,332</i>	<i>-</i>	<i>21,829</i>	<i>45,365</i>	<i>-</i>

(CHF thousands)	Positive replacement values (cumulative)	Negative replacement values (cumulative)
<b>Total after netting agreements</b>	<b>54,679</b>	<b>29,382</b>
Total previous year	24,353	47,697

### Breakdown by counterparty

(CHF thousands)	Central clearing houses	Banks and securities dealers	Other customers
Positive replacement values (after netting agreements)	-	54,152	527

There were no netting contracts on derivative financial instruments open as at 31.12.2017 and 31.12.2016.

## 5.6.5 Breakdown of financial investments

(CHF thousands)	Book value		Fair value	
	31.12.2017	31.12.2016	31.12.2017	31.12.2016
Debt securities	250,283	261,571	251,902	263,287
<i>of which intended to be held to maturity</i>	250,283	261,571	251,902	263,287
<i>of which not intended to be held to maturity (available for sale)</i>	-	-	-	-
Shares in investment funds	26,885	27,616	27,696	27,787
Equity-type securities	9,830	171	10,261	369
<i>of which qualified participations (at least 10% of voting capital)</i>	-	-	-	-
Precious metals	126	146	126	146
Real estate	1,363	1,450	1,363	1,450
<b>Total financial investments</b>	<b>288,487</b>	<b>290,954</b>	<b>291,348</b>	<b>293,039</b>
<i>of which securities eligible for repo transactions in accordance with liquidity requirements</i>	153,002	143,591	154,442	145,804

## Breakdown of counterparties by rating

(CHF thousands)	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	Below B-	Unrated
Book value of debt securities	178,273	28,589	23,183	-	-	20,238

The valuations are based on ratings by Standard & Poor's.

## 5.6.6 Breakdown of other assets and other liabilities

(CHF thousands)	31.12.2017	31.12.2016
<b>Other assets</b>		
Compensation account	6,365	11,747
Indirect taxes	611	575
Various other assets	10,336	263,688 <sup>1</sup>
<b>Total other assets</b>	<b>17,312</b>	<b>276,010</b>
<b>Other liabilities</b>		
Direct / indirect taxes	4,425	5,089
Unredeemed cash bonds	2,312	2,903
Various other liabilities	117,189 <sup>2</sup>	2,658
<b>Total other liabilities</b>	<b>123,926</b>	<b>10,650</b>

<sup>1</sup> of which a balance of CHF 261 million for in-house banking transactions.

<sup>2</sup> of which CHF 91.1 million from in-house banking operations and CHF 23.4 million additional payment to the Canton for 2016.

### 5.6.7 Disclosure of assets pledged or assigned to secure own commitments and of assets under reservation of ownership

(CHF thousands)	31.12.2017		31.12.2016	
	Book value	Effective commitments	Book value	Effective commitments
<b>Pledged / assigned assets</b> (excluding advances and repurchase agreements with securities)				
Book value of mortgages set as collateral for bonds and loans with the SCB Central	2,501,045	2,042,000	2,450,430	1,968,000
Book value of securities delivered as collateral to SIX Group AG	1,417	-	1,818	-
Book value of securities delivered as collateral in connection with Repo Light credit with the SNB	23,503	-	22,325	-
Book value of assets pledged to secure own commitments	1,241	1,241	5,345	5,345
<b>Total pledged / assigned assets</b>	<b>2,527,206</b>	<b>2,043,241</b>	<b>2,479,918</b>	<b>1,973,345</b>
<b>Assets under reservation of ownership</b> Assets under reservation of ownership	-	-	-	-

### 5.6.8 Disclosure of the economic position of own pension schemes

#### 5.6.8.1 Disclosure of liabilities relating to own pension schemes, and number and nature of equity instruments of the Bank held by own pension schemes

The Bank has no obligations towards pension schemes.

#### 5.6.8.2 Disclosures on the economic situation of own pension schemes

##### a) Employer contribution reserves (ECR)

The Bank had no ECR as at 31.12.2017.

##### b) Presentation of the economic benefit / obligation and the pension expenses

	Over- / underfunding at the end of 2017	Economic interest of the Bank		Change in economic interest (benefit and/or commitment) versus previous year	Contributions paid for 2017	Pension expenses in personnel expenses	
		31.12.2017	31.12.2016			31.12.2017	31.12.2016
Pension plans without overfunding / underfunding	-	-	-	-	7,725	7,778	6,626

Contributions are paid to the insurance company. The employer's contributions are carried under "Personnel expenses".

The Bank has opted for affiliation to the Group Plan LPP Swiss Life, a legally independent pension fund. The pension plan is a defined-contribution scheme and provides the basic compulsory coverage as stated in the Swiss LPP (Federal Law on Occupational Benefits), as well as complementary coverage.

At the end of the accounting period the Bank had no obligation towards the pension funds. There are no contribution reserves on the part of the employer and the relationship between the Bank and its pension fund is based on a global affiliation contract.

The pension fund reinsures all pension risks by means of a comprehensive insurance contract. Within the framework of this contract, no possibility of underfunding exists and, consequently, there are no obligations in this regard on the part of the employer.

### 5.6.9 Presentation of value adjustments, provisions and reserves for general banking risks and changes in the current year

(CHF thousands)	Status 31.12.2016	2017					Status 31.12.2017
		Use in conformity with designated purpose	Currency differences	Past due interest and recoveries	New creations charged to income	Releases to income	
<b>Provisions</b>							
Provisions for default risk	277	-10	-	-	24	-252	39
Value adjustments and provisions for other operating risks	491	-32	-	-	-	-	459
Additional pension provision	2,400	-783	-	-	485	-	2,102
Other provisions	157	-	-	-	-	-157	-
<b>Total provisions</b>	<b>3,325</b>	<b>-825</b>	<b>-</b>	<b>-</b>	<b>509</b>	<b>-409</b>	<b>2,600</b>
<b>Reserves for general banking risks</b>	<b>411,886</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>26,114</b>	<b>-</b>	<b>438,000</b>
<b>Value adjustments for default and country risks</b>	<b>55,247</b>	<b>-836</b>	<b>-167</b>	<b>-</b>	<b>20,544</b>	<b>-12,725</b>	<b>62,063</b>
of which value adjustments for default risk from impaired loans	55,247	-836	-167	-	20,544	-12,725	62,063

### 5.6.10 Presentation of the Bank's endowment capital

(CHF thousands)	31.12.2017			31.12.2016		
	Total par value	Quantity	Capital eligible for dividend	Total par value	Quantity	Capital eligible for dividend
<b>Endowment capital</b>						
Endowment capital	300,000	300,000	300,000	240,000	240,000	240,000
of which paid up	300,000	300,000	300,000	240,000	240,000	240,000
<b>Total endowment capital</b>	<b>300,000</b>	<b>300,000</b>	<b>300,000</b>	<b>240,000</b>	<b>240,000</b>	<b>240,000</b>

On 19 June 2017, the Grand Council (Cantonal Parliament) approved a request for an increase of the endowment capital from CHF 240 million to CHF 500 million. This increase was granted with the transformation into endowment capital of perpetual subordinated loans for a total of CHF 140 million and the authorisation to increase the capital by an additional CHF 120 million. The Bank did not issue participations.

### 5.6.11 Disclosure of amounts due from / to related parties

(CHF thousands)	31.12.2017		31.12.2016	
	Due from	Due to	Due from	Due to
Holders of qualified participations	12,000	181,913	12,000	227,514
Group companies	71,863	232,482	38,501	113,698
Linked companies	10,316	123,960	10,300	153,618
Transactions with members of governing bodies	109,744	6,957	93,674	6,500

The amounts indicated include any off-balance sheet operation that may have been effected. Loans to companies or entities related to the Canton consist of operating and investment loans granted on the basis of standard lending parameters. Receivables from and payables to companies or entities related to the Canton are concluded at market conditions. Loans to governing bodies primarily consist of mortgage loans and are concluded at market conditions.

## 5.6.12 Disclosure of holders of significant participations

(CHF thousands)	31.12.2017		31.12.2016	
Holders of significant participations	Nominal	% of equity	Nominal	% of equity
Canton Ticino With voting rights	300,000	100	240,000	100

## 5.6.13 Breakdown of total assets by credit rating of country groups (risk domicile view)

Bank's own country rating (CHF thousands)	Rating Standard & Poor's	31.12.2017		31.12.2016	
		Net foreign exposure	Share as %	Net foreign exposure	Share as %
1 Excellent and high quality	AAA to AA-	289,146	82.8%	238,395	84.2%
2 Above-average quality	A+ to A-	2,028	0.6%	2,251	0.8%
3 Average quality	BBB+ to BBB-	47,564	13.6%	36,188	12.8%
4 Risk of default	BB+ to BB	804	0.2%	837	0.3%
5 Significant risk of default	BB-	1,305	0.4%	1	0.0%
6 Speculative, high risk of default	B+ to B-	1	0.0%	59	0.0%
7 Poor quality, very high risk	CCC+ to D	-	0.0%	-	0.0%
Unrated		8,287	2.4%	5,277	1.9%
<b>Total</b>		<b>349,135</b>	<b>100.0%</b>	<b>283,008</b>	<b>100.0%</b>

The breakdown by domestic and foreign origin is made on the basis of the customer's domicile, with the exception of mortgage loans where the domicile of the property is the relevant criterion. Liechtenstein is deemed to be a foreign country.

Standard & Poor's ratings have been used since 2017. Previous year values have been reclassified to ensure comparability.

## 5.7 INFORMATION ON OFF-BALANCE SHEET TRANSACTIONS

### 5.7.14 Breakdown of fiduciary transactions

(CHF thousands)	31.12.2017	31.12.2016
Fiduciary investments	38,899	15,003
<b>Total fiduciary transactions</b>	<b>38,899</b>	<b>15,003</b>

## 5.8 INFORMATION ON THE INCOME STATEMENT

### 5.8.15 Breakdown of the result from trading activities and fair value option

(CHF thousands)	2017	2016
Result from trading activities from:		
Foreign currencies	9,860	11,712
Banknote trading	3,181	822
Commodities / precious metals	1,292	1,173
Securities trading	393	-401
<b>Total result from trading activities</b>	<b>14,726</b>	<b>13,306</b>

### 5.8.16 Disclosure of material refinancing income in the item Interest and discount income as well as material negative interest

Refinancing income in the item "Result from interest operations"		
Income and dividend income from trading portfolio is offset with costs of refinancing of that portfolio.		
(CHF thousands)	2017	2016
<b>Negative interest</b>		
Negative interest on assets (decrease in interest and discount income)	62	152
Negative interest on commitments (decrease in interest expenses)	3,979	3,141

### 5.8.17 Breakdown of personnel expenses

(CHF thousands)	2017	2016
Salaries	53,191	51,379
<i>of which expenses relating to share-based compensation and alternative forms of variable compensation</i>	-	-
Social benefits	13,078	11,311
Other personnel expenses	2,260	2,216
<b>Total personnel expenses</b>	<b>68,529</b>	<b>64,906</b>

### 5.8.18 Breakdown of other operating expenses

(CHF thousands)	2017	2016
Office space expenses	4,992	5,048
Expenses for information and communications technology	17,082	15,488
Expenses for vehicles, equipment, furniture and other fixtures as well as operating lease expenses	398	325
Fees of audit firm	476	496
<i>of which for financial and regulatory audits</i>	456	446
<i>of which for other services</i>	20	50
Other operating expenses	10,411	10,988
<i>of which compensation for any State guarantee</i>	-	-
<b>Total other operating expenses</b>	<b>33,359</b>	<b>32,345</b>

### 5.8.19 Explanations regarding material losses, extraordinary income and expenses, material releases of hidden reserves, reserves for general banking risks, and value adjustments and provisions no longer required

<p><b>5.8.19.1 Material losses</b> No material losses were incurred during the financial year.</p>
<p><b>5.8.19.2 Extraordinary income and extraordinary expenses</b> The extraordinary amount of CHF 2.5 million is mainly due to the proceeds from the variable component of the sales price of our participation in Swisscanto Holding AG which was concluded in 2015.</p>
<p><b>5.8.19.3 Hidden reserves</b> The Bank does not hold any hidden reserve, and presents its individual financial statements in accordance with the true and fair view principle.</p>
<p><b>5.8.19.4 Reserves for general banking risks</b> CHF 26.1 million were deducted from "Changes in reserves for general banking risks" and allocated to reserves for general banking risks.</p>
<p><b>5.8.19.5 Value adjustments and provisions no longer required</b> There is no relevant information to be provided under this heading.</p>
<p><b>5.8.19.6 Revaluations of participations and tangible fixed assets</b> There were no revaluations of participations or tangible fixed assets during the financial year.</p>

### 5.8.20 Presentation of current and deferred taxes, and disclosure of tax rate

(CHF thousands)	31.12.2017	31.12.2016
Real estate tax	317	266
Provisions for deferred taxes	-	-
<b>Total taxes</b>	<b>317</b>	<b>266</b>

The Bank is exempt from federal, cantonal and communal taxation. It is subject to real estate taxation.



## **Report of the auditor to the Council and to the Cantonal Parliament of the Republic and Canton of Ticino, Bellinzona**

### **Report on the audit of the financial statements**

#### **Opinion**

We have audited the financial statements of Banca dello Stato del Cantone Ticino, which comprise the balance sheet as at 31 December 2017, income statement, statement of changes in equity and notes for the year then ended, including a summary of significant accounting policies (pages 78-92).

In our opinion, the financial statements as at 31 December 2017 give a true and fair view of the financial position, the results of operations and the cash flow in accordance with accounting rules for banks and comply with Swiss law and the Law on Banca dello Stato del Cantone Ticino.

#### **Basis for opinion**

We conducted our audit in accordance with Swiss law and Swiss Auditing Standards. Our responsibilities under those provisions and standards are further described in the "Auditor's responsibilities for the audit of the financial statements" section of our report.

We are independent of the entity in accordance with the provisions of Swiss law and the requirements of the Swiss audit profession and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **Our audit approach**

##### **Overview**



- Overall materiality: CHF 3.5 million
- We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the financial statements as a whole, taking into account the structure of the entity, the accounting processes and controls, and the industry in which the entity operates.

As key audit matter the following area of focus has been identified:

- Impairment of amounts due from customers and mortgage loans

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PricewaterhouseCoopers SA is a member of the global PricewaterhouseCoopers network of firms, each of which is a separate and independent legal entity.



### ***Audit scope***

We designed our audit by determining materiality and assessing the risks of material misstatement in the financial statements. In particular, we considered where subjective judgements were made; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

### ***Materiality***

The scope of our audit was influenced by our application of materiality. Our audit opinion aims to provide reasonable assurance that the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall materiality for the financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

<i>Overall materiality</i>	CHF 3.5 million
<i>How we determined it</i>	5% of the operating result (result of the period before tax, changes in reserves for general banking risks and extraordinary items).
<i>Rationale for the materiality benchmark applied</i>	We chose the operating result (result of the period before tax, changes in reserves for general banking risks and extraordinary items) because it is the benchmark against which the performance of a bank is most commonly measured and it is the generally accepted benchmark in the financial industry.

We agreed with the Audit Committee of the Board of Directors that we would report to them misstatements above CHF 173'500 identified during our audit as well as any misstatements below that amount which, in our view, warranted reporting for qualitative reasons.

### ***Report on key audit matters based on the circular 1/2015 of the Federal Audit Oversight Authority***

Key audit matters are those matters that, in our professional judgement, 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 of amounts due from customers and mortgage loans

<i>Key audit matter</i>	<i>How our audit addressed the key audit matter</i>
<p>As shown in the note 5.6.2 of the annual report 2017, the Bank grants loans and advances to customers and mortgage loans (83% of total assets or CHF 10'428 million). We consider the valuation of amounts due from clients and mortgage loans that show signs of potential default to be a key audit matter on the basis of the significance of the related balance sheet positions. Moreover, the determination of the amount of any write-down is based on the debtor's capacity to repay the amount due and/or the liquidation value of the collateral, both of which may be influenced by subjective factors.</p> <p>The Bank has a control system in place that enables its various governing bodies to identify and to analyze the risk of default, to take precautionary measures and to calculate the necessary impairment charges.</p> <p>The accounting and valuation principles for amounts due from clients and the methods used to identify default risks and determine the need for impairment are described in the notes to the consolidated financial statements (sections 5.2.3.3, 5.4.1 and 5.5).</p>	<p>We checked and tested the key controls relating to credit transactions:</p> <ul style="list-style-type: none"><li>• controls aimed to identify signs of potential default in order to determine the scope of non-performing and/or impaired loans;</li><li>• controls relating to the calculation of value adjustment including the determination of the market value of the collaterals.</li></ul> <p>In addition, we checked on a sample basis that:</p> <ul style="list-style-type: none"><li>• the risk category given to the selected credit was adequate;</li><li>• the market value of the collateral was determined or updated in accordance with market practice;</li><li>• the value adjustments and provisions were calculated and recorded in accordance with the accounting principles.</li></ul> <p>On the basis of our audit procedures, we consider the valuation of amounts due from clients and mortgage loans to be adequate.</p>

### Responsibilities of the Board of Directors for the financial statements

The Board of Directors is responsible for the preparation of the financial statements that give a true and fair view in accordance with accounting rules for banks, the provisions of Swiss law and the Law on Banca dello Stato del Cantone Ticino, and for such internal control as the Board of Directors 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, the Board of Directors is responsible for assessing the entity'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 the Board of Directors either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so.

### Auditor's 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 auditor's 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 Swiss law and Swiss Auditing Standards 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 Swiss law and Swiss Auditing Standards, we exercise professional judgment and maintain professional scepticism 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 entity's internal control;
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made;
- Conclude on the appropriateness of Board of Directors' 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 entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's 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 auditor's report. However, future events or conditions may cause the entity to cease to continue as a going concern.

We communicate with the Board of Directors or its relevant committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Board of Directors or its relevant committee with a statement that we have complied with relevant ethical requirements regarding independence, and to 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 the Board of Directors or its relevant committee, 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 auditor's 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 on other legal and regulatory requirements***

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system exists which has been designed for the preparation of financial statements according to the instructions of the Board of Directors.

We further confirm that the proposed appropriation of available earnings complies with Swiss law and the company's articles of incorporation. We recommend that the financial statements submitted to you be approved.

PricewaterhouseCoopers Ltd

A handwritten signature in blue ink, appearing to read 'Glenda Braendli', written over a faint, illegible stamp.

Glenda Braendli  
Audit expert  
Auditor in charge

A handwritten signature in blue ink, appearing to read 'Lorenzo Morelli', written over a faint, illegible stamp.

Lorenzo Morelli  
Audit expert

Lugano, 27 March 2018

# I. Information on Capital Adequacy Basel III and on Liquidity (unaudited data)

## Methods used for the calculation of capital adequacy requirements

- **Credit risk:** international approach (SA-BIS).
- **Market risk:** standardised approach for market risks.
- **Operational risks:** basic indicator approach.

## I.I PRESENTATION OF RECOGNISED REGULATORY CAPITAL

(CHF thousands)	31.12.2017	31.12.2016	Notes
Bank's endowment capital	300,000	240,000	I.II
Statutory retained earnings reserve	252,074	240,028	I.II
Reserves for general banking risks	438,000	411,886	I.II
<b>Total common equity Tier 1 capital</b>	<b>990,074</b>	<b>891,914</b>	
Other elements to be deducted from common equity capital	-83,910	-83,909	I.II
<b>Total common equity Tier 1 capital (net CET1)</b>	<b>906,164</b>	<b>808,005</b>	
Additional Tier 1 capital (AT1)	80,000	140,000	I.II
<b>Total net Tier 1 capital</b>	<b>986,164</b>	<b>948,005</b>	
Tier 2 capital (T2)	87,500	105,000	I.II
<b>Total regulatory capital</b>	<b>1,073,664</b>	<b>1,053,005</b>	
<b>Total risk-weighted positions</b>	<b>6,508,970</b>	<b>6,249,214</b>	

## I.II RATIOS

(as a % of risk-weighted positions)	31.12.2017
Net CET1 ratio	13.9%
Net Tier 1 ratio	15.2%
Total regulatory capital ratio	16.5%
CET1 requirements under the terms of CAO transitional provisions	8.2%
<i>of which capital buffer</i>	2.9%
<i>of which countercyclical capital buffer (% of risk-weighted positions)</i>	0.8%
CET1 available for the coverage of minimum requirements and buffers, after deduction of AT1 and T2 requirements covered by CET1	13.0%
CET1 target based on FINMA Circular 11/2 "Capital buffer and capital planning" plus countercyclical capital buffer	8.2%
Available CET1	12.7%
T1 target based on FINMA 11/2 plus countercyclical buffer	9.8%
Available T1	14.3%
Regulatory capital target based on FINMA Circular 11/2 plus countercyclical buffer	12.0%
Available regulatory capital	16.5%

### I.III EVERAGE RATIO AND CALCULATION OF GLOBAL EXPOSURE SUBJECT TO LEVERAGE RATIO

(CHF thousands)		31.12.2017	31.12.2016
<b>1</b>	<b>Global exposure subject to leverage effect (vs. assets in balance sheet)</b>	<b>12,866,652</b>	<b>12,542,534</b>
+	Total assets as per disclosed Annual Report	12,613,122	12,172,995
-	Adjustments of assets deducted from Tier 1 capital and relating to entities not included in the regulatory consolidation scope	-83,910	-83,910
+	Adjustments on derivative financial instruments	40,262	38,351
+	Adjustments relating to securities financing transactions	1,504	124,621
+	Adjustments relating to off-balance sheet transactions	295,674	290,477
<b>2</b>	<b>Global exposure subject to leverage effect ratio</b>	<b>12,866,652</b>	<b>12,542,534</b>
<b>2.1</b>	<b>Balance sheet exposure</b>	<b>12,474,534</b>	<b>12,064,732</b>
+	Balance sheet exposure excluding derivatives and securities financing transactions	12,558,444	12,148,642
-	Assets deducted from considered Tier 1 capital	-83,910	-83,910
<b>2.2</b>	<b>Derivative exposure</b>	<b>94,941</b>	<b>62,704</b>
+	Positive replacement value of all derivative transactions taken into consideration margin payments	54,679	24,353
+	Add-ons in relation to all derivatives	40,262	38,351
<b>2.3</b>	<b>Exposure relating to securities financing transactions</b>	<b>1,504</b>	<b>124,621</b>
<b>2.4</b>	<b>Other off-balance sheet exposures</b>	<b>295,673</b>	<b>290,477</b>
+	Off-balance sheet exposure at gross nominal value before credit conversion factor	1,772,073	1,813,264
-	Adjustment after credit conversion factor	-1,476,400	-1,522,787
<b>3</b>	<b>Net Tier 1 capital</b>	<b>986,164</b>	<b>948,005</b>
<b>4</b>	<b>Basel III leverage ratio</b>	<b>7.7%</b>	<b>7.6%</b>

### I.IV INFORMATION ON LIQUIDITY COVERAGE RATIO (LCR)

(CHF thousands)	Q1 2017 <sup>1</sup>	Q2 2017 <sup>1</sup>	Q3 2017 <sup>1</sup>	Q4 2017 <sup>1</sup>
High quality liquid assets (HQLA) <sup>2</sup>	1,297,843	1,262,034	1,262,524	1,316,738
of which level 1 assets	1,177,193	1,152,984	1,148,772	1,199,148
of which level 2 assets	120,650	109,050	113,752	117,590
Net outflows	1,183,597	1,230,190	1,108,221	910,533
<b>Short-term liquidity coverage ratio</b>	<b>110%</b>	<b>103%</b>	<b>114%</b>	<b>145%</b>
Previous year	87%	115%	140%	141%

<sup>1</sup> Average for the quarter, calculated on the basis of monthly statistics.

<sup>2</sup> In accordance with FINMA regulatory requirements, refer to Circular 2015/2 "Liquidity Risks - banks"

### I.V INFORMATION ON THE CALCULATION OF CAPITAL

The disclosure obligations stated in FINMA Circular 2016/1 "Disclosure - banks" are adhered to on a consolidated basis. This information is published in the 2017 Annual Report of the BancaStato Group ([www.bancastato.ch](http://www.bancastato.ch)).

# Board of Directors

at 31.12.2017

# Public Mandate Control Commission

at 31.12.2017

## Chairman

Bernardino Bulla

## Chairman

Nicola Brivio

## Deputy Chairman

Carlo Danzi<sup>1</sup>

## Deputy Chairman

Pelin Kandemir Bordoli

## Secretary

Raoul Paglia<sup>1,2</sup>

## Members

Maurizio Agustoni

Omar Balli

Claudia Crivelli Barella

Gabriele Pinoja

## Members

Marco Fantoni<sup>1</sup>

Avv. Giovanni Jelmini<sup>1,2</sup>

Michele Morisoli<sup>1,2</sup>

Luca Soncini<sup>1</sup>

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<sup>1</sup> Independent members as specified in FINMA Circular 2017/01

<sup>2</sup> Members of the Audit and Risk Committee

# External Auditors as defined by the Swiss Federal Law on Banks and Savings Banks

PricewaterhouseCoopers SA

# Internal Auditors

## **Head of Internal Auditors**

Gabriele Guglielmini

## **Deputy**

Guido Gianetti

# Executive Board

at 31.12.2017

## President of the Executive Board

Fabrizio Cieslakiewicz

## Members of the Executive Board

Daniele Albisetti

Claudio Genasci

Patrick Lafranchi

Gabriele Zanzi

# Members of the Management

at 31.12.2017

## Bellinzona Branch

Domenico Albertoni

Romano Bär

Mauro Bazzotti

Lucamaria Beeler

Enrico Bertozzi

Luca Bordonzotti

Omar Cadola

Dario Caramanica

Medardo Caretti

Curzio De Gottardi

Maurizio Derada

Adolfo Genzoli

Luca Ghiringhelli

Manuel Giambonini

Clio Indemini

Gabrio Lavizzari

Daniele Manzoni

Raffaele Marti

Roberto Meyer

Marco Molteni

Massimiliano Morelli

Roberto Nuschak

Massimo Penzavalli

Ivo Pini

Giulio Ruggeri

Giorgio Sala

Michele Schandroch

Lorenzo Squellati

Norman Stampanoni

Fabrizio Stöckli

Carlo Tomasini

Ferruccio Unternährer

Mirko Zoppi

## Lugano Branch

Roberto Barbera

Filippo Dotti

Andrea Ferrari

Luigi Longoni

Gabriele Mantegazzi

Alberto Pedrazzi

Carlo Ruggia

Luca Todesco

Jvan Zatta

## Locarno Branch

Boris Ceschi

Fabrizio Conti-Rossini

Verena Gaggetta

Claudio Gnesa

Stephan Mair

Marco Meschiari

Marco Pellanda

Franco Storni

## Chiasso Branch

Claudio Cereghetti

Mario Grassi

Lorenzo Imperiali

Gilberto Pittaluga

Marco Soragni

## Head Office

Viale H. Guisan 5  
Casella Postale  
**6501 Bellinzona**

## Branches

Corso S. Gottardo 4  
**6830 Chiasso**

Via Naviglio Vecchio 4  
**6600 Locarno**

Via Pioda 7  
**6900 Lugano**

# Agencies

Via Cantonale

**6982 Agno**

**6780 Airolo**

Viale Papio 5

**6612 Ascona**

Via Pini 2

**6710 Biasca**

Via Leoncavallo

**6614 Brissago**

Via Pretorio 3

**6675 Cevio**

**6715 Dongio**

Piazza S. Franscini 5

**6760 Faido**

Largo Libero Olgiati 81a

**6512 Giubiasco**

Via San Gottardo 77

**6596 Gordola**

Via Trevano 97

**6904 Lugano-Molino Nuovo**

**6900 Lugano-Piazza Riforma**

Via Pobiette 1

**6928 Manno**

Via Lavizzari 18

**6850 Mendrisio**

Via Pietro Fontana

**6950 Tesserete**

## ONLINE AGENCY

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agenziavicino@bancastato.ch

c/o Bank Headquarters

## ATM ONLY

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**6500 Bellinzona**

Piazza Collegiata

**6500 Bellinzona**

Via San Francesco 1

**6600 Locarno-Città vecchia**

Via Emmaus 1

(Centro Comm. Cattori)

**6616 Losone**

Ospedale Civico

**6900 Lugano**

Via Turconi 23

**6850 Mendrisio**

Via Cantonale 19

**6805 Mezzovico**

Via alle Brere 5

**6598 Tenero**

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Tel 091 803 71 11

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