IOR Istituto per le Opere di Religione

Annual Report 2017

Istituto per le Opere di Religione
Cortile Sisto V
00120 Vatican City State
Vatican City State

Registered under No 1 in the Register of Legal Persons
held at “Governatorato” of Vatican City State

Authorization n. 1 of 10/07/2015 issued by AIF,
to carrying out in professional way financial activities at Vatican City State

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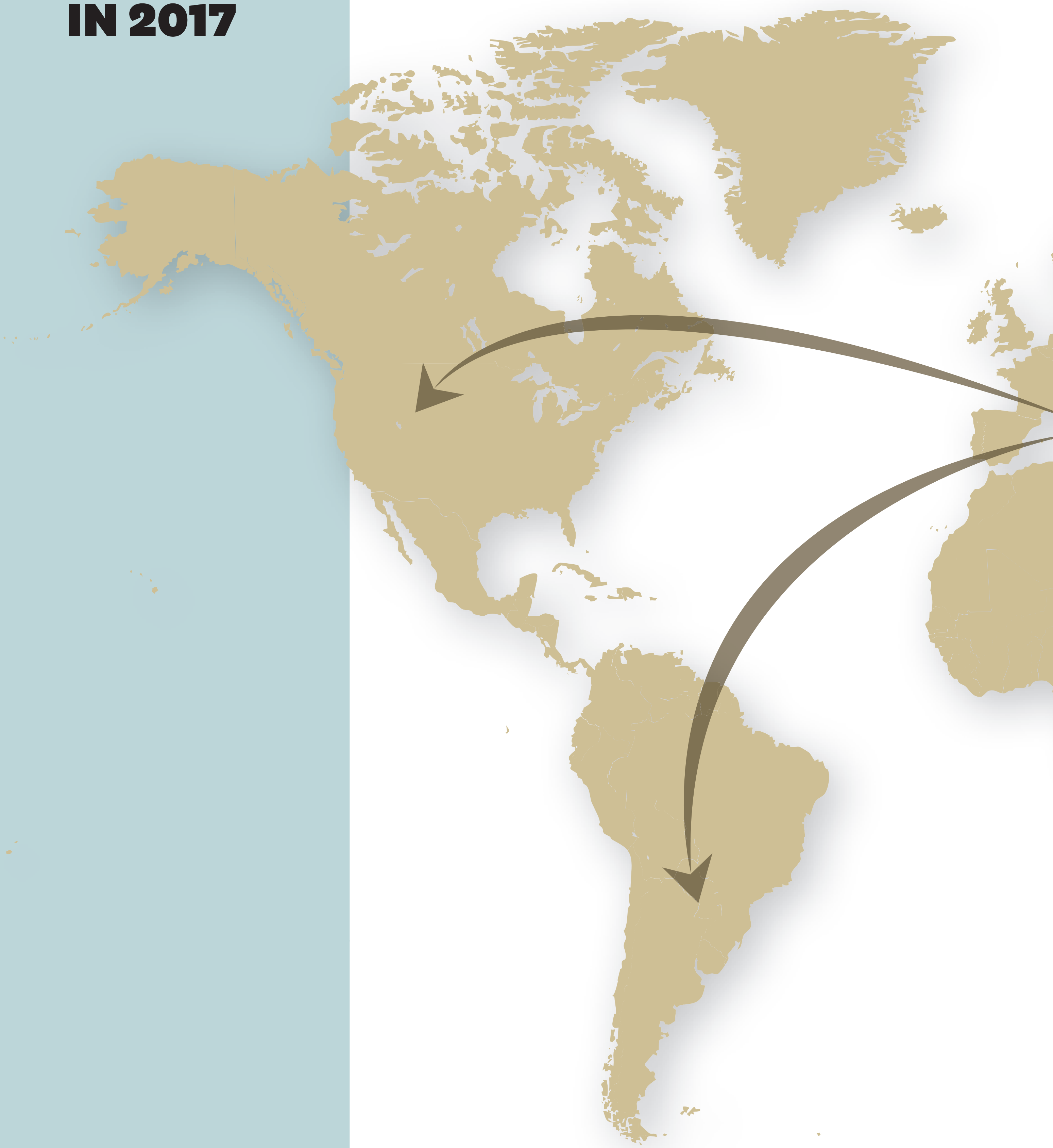
Money must serve not rule

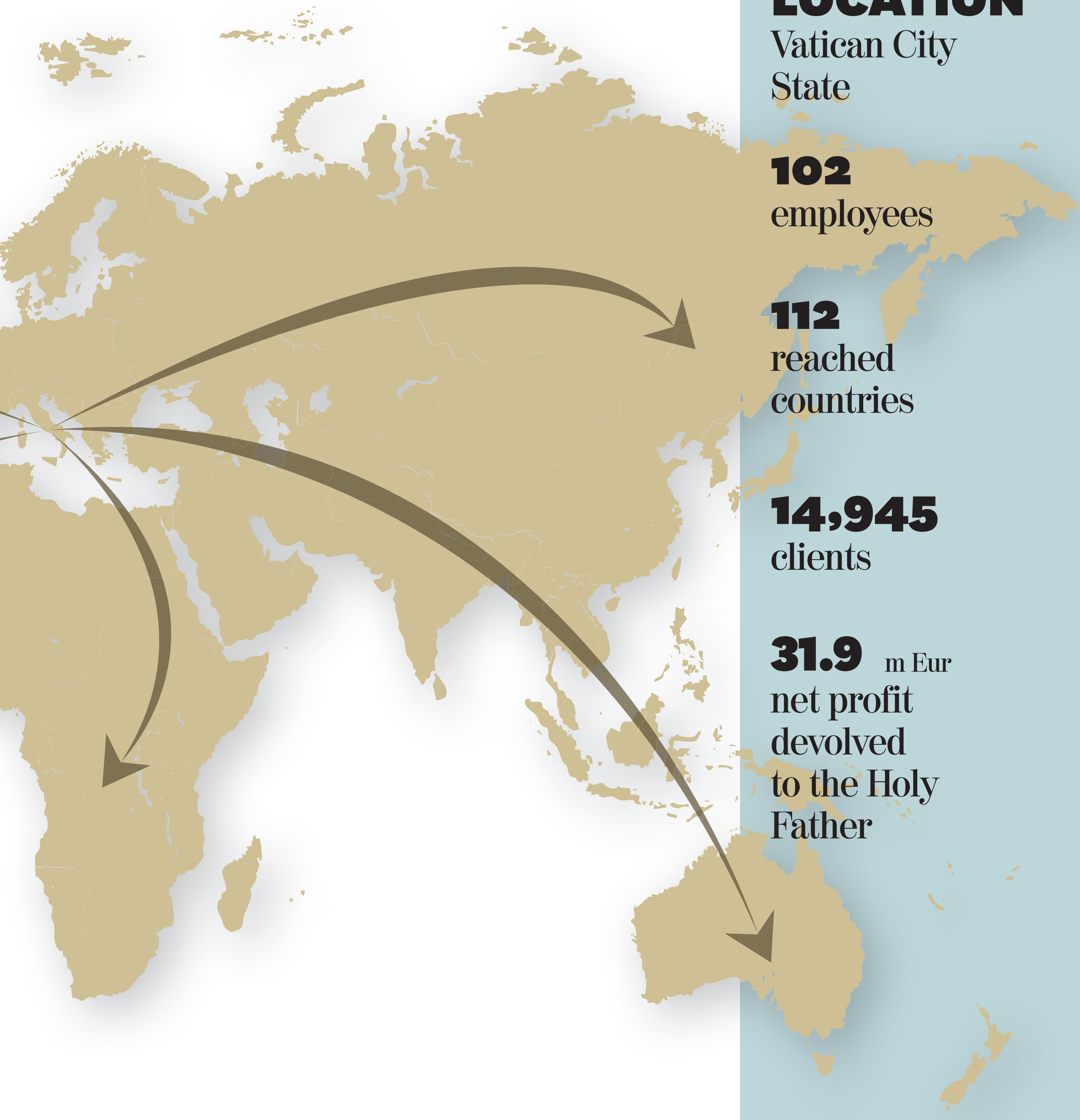
His Holiness
Pope Francis,
Evangelii Gaudium, 2013

AT THE SERVICE OF THE CATHOLIC

IOR
IN 2017



CHURCH ALL OVER THE WORLD



SINGLE LOCATION
Vatican City State

102
employees

112
reached countries

14,945
clients

31.9 m Eur
net profit devolved to the Holy Father

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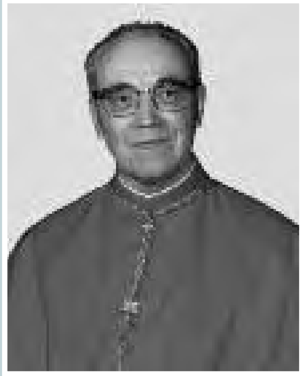
The present Annual Report has been translated from the original one which is prepared in Italian

President of the Commission of Cardinals' message



Cardinal Santos Abril y Castelló
President of the Commission of Cardinals

The time has come for the Institute to present - for the sixth consecutive year - the annual financial statements for the 2017 fiscal year, which closed with a net profit of €31.9 million.

This is undoubtedly a remarkable result in light of both the strict ethical parameters within which the IOR operates, in line with its Statutes, as well as the complex geo-political and financial scenarios that characterized the global economy in 2017.

Leaving the task of analysing the genesis of said profit and its consistency with the challenging global economic environment of 2017 to the Institute's "technical experts", as President of the IOR's Supervisory Commission of Cardinals, I consider it, instead, a priority to emphasize the consistency of this result with the Institute's commitment to never subordinate the ethics of its choices to profit, in compliance with the clear directives received from the Holy Father in this regard, even when this may lead to reduced profits.

Once again, in 2017, the Institute renewed its commitment to affirm the importance of ethics over profit through key "ethical" decisions that have affected, inter alia, sensitive areas of activity such as investments, tax transparency and the legal strategy followed to protect its reputation.

In this regard, I wish to mention the Institute's choice to continue to select for itself and for its customers only investments in line with Catholic principles and its decision to fully implement the tax agreements signed in recent years with the United States of America and the Italian Republic in order to make the accounts of the Institute and those of its customers fiscally transparent, despite being aware of a possible reduction in the number of customers as a result of such rigorous choices.

Likewise, I would like to remind you of the Institute's choice to refer to the decisions of the competent courts in ascertaining the responsibilities of individuals who, in the past, while holding different positions (directors, managers, investors and/or consultants of the time), betrayed its trust and caused serious harm, in spite of the substantial settlement agreements proposed by some of the parties involved to repair the damage caused to the Institute by their conduct. Being aware of the importance of affirming, even in this case, the centrality of ethics beyond the strictly financial dimension, the Institute refused to negotiate with the people who had brought discredit upon it, instead subordinating any compensation for reputational and economic damages to the establishment of responsibilities by the competent authorities and to their decisions.

Among the relevant facts of the year, the overall positive opinion expressed in Moneyval's December 2017 report on the appropriateness of the legislative instruments and good practices already adopted by the IOR to effectively combat money laundering and terrorism is worthy of mention. Recognition by this prestigious European body of the progress the Institute has made in such a sensitive sector has been a valuable incentive for the latter to continue with renewed determination in the improvement of the existing legislative instruments and practices that is already underway.

Lastly, the process of reform of the Statutes is reaching its conclusion and it is to be expected that the reformed Statutes and the Institute's new regulation will be adopted in the near future, in compliance with the Holy Father's request to provide the Institute with transparent, effective and modern instruments of governance.

Santos Card. Abril

Msgr. Battista Mario Salvatore Ricca
Prelate

Prelate's message

This year, as in the past, I would like to take advantage of the publication of the Financial Statements to convey a few words, simply, without claiming to have any technical competence, to all those who work conscientiously and with professionalism, and have enabled the Institute for the Works of Religion to continue along the road towards a change of mindset in working and recovering a more precise understanding of the aims of the Institute.

Change of mindset: one should not work at the Institute and think it's like working at any one place. In the past, this led us to take approaches that were a bit too breezy and not always careful about ethics, in the absence of which, an excessive independence had been reached, which threatened to make us lose sight of the meaning of the real need of the Institute, and therefore its usefulness for the Holy See. The wise guidance of the President and the Director and everyone's willingness to question themselves has already produced fruits that are there for all to see.

A more precise understanding of the goals: the results of the financial statements show that the logic of making money for the sake of it has gone by, and money is to be used to meet the needs for which the Institute was founded, i.e. help the activities of the Catholic Church. It is often believed that if one has so much, one can do a lot. It's better to own little and do well, do necessary things, and redesign priorities. The Scripture warns: "Better is a little to the just, than the great riches of the wicked." Psalm 36:16, and again: "He who loves money will not be satisfied with money, nor he who loves abundance with its income. This too is vanity." Ecclesiastes 5:9. In addition to the Bible, even the way we all think makes us believe that if we had twice the money and twice the possibilities, we would complain that they are not enough, while reality shows us every day that with half of what we have, we do the same things.

I am sure that we will continue along this pathway and wish everyone to continue giving the best that everyone can give with enthusiasm.

IOR

Istituto per le Opere di Religione

Management Report

Chapter 1
Strategic information

Jean-Baptiste Douville de Franssu
President of the Board of Superintendence

1. PRESIDENT OF THE BOARD OF SUPERINTENDENCE'S MESSAGE

Since its appointment in July 2014, the Board of Superintendence has worked on the necessary transformation of the IOR to serve with prudence the Holy Father in fulfilling his mission as Universal Pastor. The appointment of three new Members in 2016, enriched the expertise, experience, and diversity of the Board.

In 2017, in a complex financial environment, much was accomplished and the Board continued to dedicate itself to the nature and the quality of the services offered to clients and to the Church. It has also furthered its efforts to consolidate its governance, reinforce internal controls, and guarantee unceasing respect for the laws and applicable regulations.

Overview

I believe there are four principal sectors that best evidence this progress:

First, controls were reinforced in the risk management and compliance function, in the legal function and in the internal audit function and various initiatives were taken on to improve procedures and surveillance. New policies were adopted in accordance with AIF regulations relating to different aspects of the everyday operations of the Institute. The hiring of new senior-level executives represented an important step; they have greatly contributed to making the IOR a stronger financial institution as illustrated in the recent Moneyval Report. In addition, with the objective of consolidating all the activities done in past years, at the initiative of the Audit and Risk Committee, the AML (Anti-money laundering) and KYC (Know your customer) procedures were reviewed by an external consultant to ensure that the IOR meets the highest international standards. Likewise, a review of the treasury operations was conducted to ensure that best practices are established and adhered to in a critical area of the Institute. When it comes to past abuses that affected IOR, a new momentum has been set with legal actions initiated in Malta related to financial products in which IOR invested in between 2011-2013, and in the Vatican, against some of former IOR managers and Board members. These developments must not be underestimated: based on four years of thorough investigative work, these are further examples of the progress completed in the reform of the Institute.

Second, the Directorate has focused its efforts to improve the quality of the products and services offered by IOR. This is the case for Asset Management solutions, where a rationalization effort has taken place to focus on major investment strategies to best serve IOR clients, improve efficiency and reduce relevant operational risks. In addition, further developments were made with regard to Catholic ethical investment principles. In 2018, the Board approved a Faith Based approach to apply to all its financial investment. Moreover, in 2018, one should start to see the fruits of the work started by the Business Transformation Strategy committee of the Board to identify further structural steps that need to be taken as to generate further growth in the Asset Management sector. In addition, the process for the

FINANCIALS 2017

5.3 bn Eur
Total client assets

103,000
Payment transactions

659.1 m Eur
Net equity

68.26%
Core equity TIER 1

Vatican City State and IOR to adhere to SEPA has started: by joining SEPA, the IOR will have access to the European payment system. This will bring more efficient and reliable procedures and be a source of savings for IOR clients. It is also appropriate to mention all the efforts that took place on the tax side over the last three years, which reached a point of final implementation in 2017. This work comes as a result of the agreements signed by the Holy See with Italy and the United States of America. It guarantees the level of transparency and stability required to build long term relationships with IOR clients and its counterparts.

Third, many aspects of the Human Resources policies were reviewed and adjusted where necessary. Among the objectives of such an exercise, one could mention the need of IOR to attract external talent as well as to contribute to the development of a new "culture" inside the Institute. This latest aspect has also been supported by the initial efforts with regard to training, very much encouraged by the HR and Remuneration committee of the Board, with the purpose of offering more opportunities to IOR staff to grow and gain further experience. Again, this is a very important step as the wellbeing and motivation of the personnel are very significant aspects considered and valued by the Board.

Finally, 2017 has continued to benefit from a favorable interest rate environment and this contributed to the delivery of a good set of results for the Institute. It is also worth mentioning, the efforts undertaken to successfully open relationships with new correspondent banks. As a consequence notably of the impact of recent Sovereign tax agreements and withdrawals to fulfil IOR's customers' charitable and missionary works, clients' assets have decreased. However, many of the previously described initiatives that will enhance the quality and reliability of IOR services will contribute to attracting new deposits.

The IOR and its personnel have made great strides over the last 12 months. However, in order that the Institute complete this ambitious task with success, the management staff must continue to be reinforced and all the efforts of the Director General of the last twelve months must be able to continue.

In all these initiatives, the Board supports the Directorate of the Institute. It will continue to provide its guidance and expertise when and where required, especially thanks to a Corporate Governance that continues to improve. Although such periods of change and transformation are never easy and bring challenges, it is fair to say that resulting from the work completed in previous years, important milestones were reached, as demonstrated clearly by the Institute's reputation significantly improving.

Approval of the 2017 accounts

After meeting with the *Revisori* and the independent audit firm, the financial statements of the Institute and the management report were approved. The proposed distribution of profits to be made to the Holy See for 2017 were discussed and approved. As per the Statute, this information was provided to the Commission of Cardinals to enable them to decide on the allocation of profits. The financial statements, prepared in accordance with IAS-IFRS, as adopted by the Circular issued by the AIF, were audited by Deloitte & Touche S.p.A.

The net result for 2017 is Euro 31.9 million. This result reflects the continuous downward trend of interest rates in Europe and the conservative approach that the Institute has adopted since 2014 in managing its assets (mainly fixed income investments). As described in the Management Report, Section 2, Part 1 - 2017 Business Review, this was achieved in a year of complex financial and political developments. This net result is in line with 2016 result and above the 2017 budget. The cost control approach adopted by the Institute had a positive contribution and IOR is now running on an annual cost base of around Euro 19 million versus Euro 20 million in 2016 and Euro 24 million in 2015 (note that 2015 operating expenses included various one-off costs).

Corporate Governance

As per the Statutes, the Board, composed of seven Members since December 2016, followed and supervised the work carried out by the Directorate in the management of the Institute.

The Board met on four occasions and various informal meetings and discussions took place. Resolutions were passed on various business matters, for which its consent was mandatory, subject to reviews and consultations in close coordination with the Directorate, as well as the Commission of Cardinals, when necessary. Once approved, the Minutes of every Board meeting were shared with the *Revisori*, the Directorate and the Prelate who were always in attendance. The Commission of Cardinals always receive copies of these acts.

The Commission of Cardinals was kept informed on every initiative and consulted as necessary on issues relating to potential changes in governance, in the IOR operating model or leadership. For example, the Board presented a proposal to the Commission of Cardinals in order to adjust the IOR Statute and to draft the first Internal Regulation.

Regular update meetings were held with the Prelate and the non-voting secretary of the Board to guarantee, among other things, an adequate flow of information.

Finally, in the first quarter of 2018, the Board asked for a review of IOR corporate governance standard to be done in line with best international practicises by a professional firm with a view to assess the Board functioning and seek possible improvements.

Board Committees

In 2015, the Board created committees to strengthen and support the governance of the Institute and the Board's work, although such committees are not provided for by the current Statute. First of all, there was the creation of the Audit and Risk Committee and the Human Resources and Remuneration Committee. In 2016, the Board created a Past Abuses Committee intended to help and support the Board in its work of understanding legacy issues and allowing for the truth to come forth. The Committee has completed its work at the end of January 2017. In 2017 a Business Transformation Strategy Committee was created to help lead the necessary changes required in terms of products and services offered to IOR clients (the composition of these committees is described below).

The meetings of the Board and the informal committees of the Board of Superintendence were held in an environment of an open exchange of information. These meetings benefitted from each member's specific expertise in various subject matters to find the appropriate resolutions to meet the needs of this unique institution. Agenda items for the meetings and materials on specific subjects important to members of the committees and the Board were distributed in advance and minutes were drafted for each meeting. At each Board meeting, a specific report was presented by the respective presidents of the committees and an annual report at year-end.

a) *Members of the Human Resources and Remuneration Committee*
Mary Ann Glendon – Chair (until February 2018)
Mauricio Larrain – Chair (from February 2018)
Jean-Baptiste Douville de Franssu (ex officio)
Scott C. Malpass (from April 2017)

b) *Members of the Audit and Risk Committee*
Sir Michael Hintze – Chair
Jean-Baptiste Douville de Franssu (ex officio)
Georg Freiherr von Boeselager (from April 2017)
Javier Marin Romano (from April 2017)

c) *Members of the Business Transformation Strategy Committee*
Scott. C. Malpass – Chair
Jean-Baptiste Douville de Franssu (ex officio)
Javier Marin Romano
Mauricio Larrain

Gian Franco Mammì, IOR Director General is always invited to participate at the committee meetings.

"Organismo di Vigilanza"

In order to comply with the provisions of Article 46 of Law VIII of the Vatican City State which provides for the creation of an "Organismo di Vigilanza", the Board of Superintendence decided to set up such a body having undertaken a thorough process to identify appropriate candidates presented by the Director General. The Body, characterized by independent decision making powers and control, has the task of supervising the operation and guaranteeing compliance with the Institute's organizational, management and control models, ensuring that they are updated and/or appropriately modified.

Acknowledgements

I would like to thank all the Board members for their support, contribution and dedication. Many of them have devoted a considerable amount of their time to help guide IOR through this transition. In early 2018, Mary Ann Glendon resigned from her position and the Board thanked her for her contribution.

In 2017, the Board has continued to work closely with the Commission of Cardinals. I wish to extend my gratitude to its President and Cardinal members for their availability and support.

I also wish to express my appreciation for the work of the Prelate, Msgr. Battista Ricca, of the Director General, Gian Franco Mammì, and to all employees of the IOR.

My gratitude, of course, also goes toward the work performed by the *Revisori* and the independent audit firm that was important for the progress achieved by IOR. Whilst the mandate of the members of the *Revisori* is coming to an end, the Board wishes to express its particular thanks for their support over the last three years.

2. MISSION, CUSTOMERS AND SERVICES

The Istituto per le Opere di Religione (the “Institute” or “IOR”) is an institution of the Holy See, founded on 27 June 1942 by Chirograph of His Holiness Pius XII. Its origins date back to the “Commissione ad Pias Causas” established by Pope Leo XIII in 1887.

The Insistute is a public legal entity according to the Canon Law (Can. 114 and 116) and carries out financial activities.

The mission of the IOR, established by its Statute, with reference to the Chirograph dated 1 March 1990 of His Holiness John Paul II, is “to provide for the custody and administration of goods transferred or entrusted to the Institute by natural or legal persons, designated for religious works or charity. The Institute can accept deposits of assets from entities or persons of the Holy See and of the Vatican City State”.

The IOR strives to serve the global mission of the Catholic Church through the administration of the entrusted assets and providing payment services to the Holy See and related entities, religious orders, other Catholic institutions, clergy, employees of the Holy See and the accredited diplomatic bodies.

The IOR is exclusively located on the sovereign territory of the Vatican City State and subject to the regulations and legislation applicable therein. The IOR is supervised and regulated by the “Autorità di Informazione Finanziaria” (AIF).

Customers of the IOR

Customers served by the Institute include:

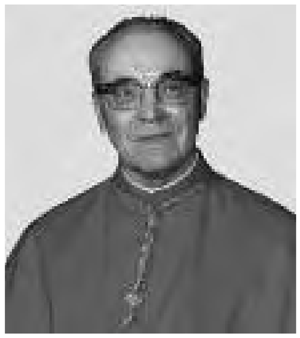
a) Institutional counterparties (Sovereign Institutions of the Holy See and Vatican City State and related entities, nunciatures and apostolic delegations, embassies and diplomats accredited to the Holy See);
b) Non-institutional counterparties (Institutes of Consecrated Life and Societies of Apostolic Life, Dioceses and other Vatican legal canonical or civil entities as legal persons; clerics and members of Institutes of Consecrated Life and Societies of Apostolic Life, employees and retirees of the Vatican as natural persons).

Most of the IOR’s clients are active in missions or perform charitable works at institutions such as schools, hospitals or refugee camps.

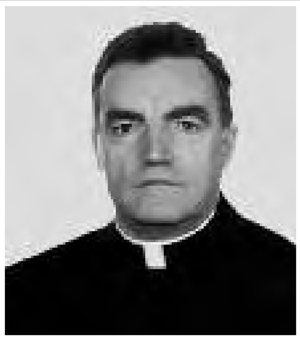
The Catholic Church, through its institutions involved in missionary activities and charitable works, is present throughout the world, even in countries with very basic infrastructure and underdeveloped banking and payment systems.

In such cases, the IOR’s services are particularly valuable. For customers located in these areas, the IOR is a bedrock, affirming itself as a trusted institution able to provide on-site services otherwise lacking or absent. This is even more evident in those geographic areas with high political financial instability.

COMMISSION OF CARDINALS CURRENT MEMBERS ARE:



Card. Santos Abril y Castelló
Archpriest *emerito* of the Papal Basilica of St. Mary Major, President of the Commission of Cardinals



Cardinal Josip Bozanic
Archbishop of Zagreb

Cardinal Thomas Christopher Collins
Archbishop of Toronto

Cardinal Pietro Parolin
Secretary of State

Nature of the Institute's services

On behalf of its clients, the Institute carries out financial activities authorized by the AIF, and offers the following services: acceptance of deposits, asset management, certain custodial functions, international payment transfers through correspondent banks, and holding salary and pension accounts of employees of the Holy See and the Vatican City State.

The Institute protects its clients' assets by primarily investing in financial instruments characterized as very low risk (e.g. government bonds, bonds issued by institutions and international organizations, as well as deposits in the interbank market).

Credit activity is residual and strictly subject to constraints of the internal policies as established by the Board of Superintendence.

No funding activities are carried out on the interbank market and IOR does not issue, underwrite or place debt securities.

Accounts opened at the IOR by authorized customers meet the requirements of the legislation on preventing and combating money-laundering and the financing of terrorism in force in the Vatican City State.

Customers are provided with services in IOR offices located in the Vatican City State. The IOR has no other locations.

3. CORPORATE GOVERNANCE

The IOR's governance structure is defined in its current Statutes. It consists of five bodies: Commission of Cardinals, Prelate, Board of Superintendence, Directorate and the *Revisori*.

The **Commission of Cardinals** oversees the Institute's adherence to its Statute. It appoints and removes members of the Board of Superintendence.

Furthermore:

– It deliberates, after considering the financial statements and taking into account IOR's own financing needs, the distribution of profits;
– It proposes to the High Authority changes to the Statutes;
– It deliberates the compensation due to members of the Board of Superintendence;
– It approves the appointment and removal of the Director General and of the Vice-Director made by the Board of Superintendence;
– Resolution of any issues concerning the members of the Board of Superintendence and the Directorate.

Members of the Commission of Cardinals are appointed for a five year term, and can be reappointed.

The current members are:

– Cardinal Santos Abril y Castelló, Archpriest *emerito* of the Papal Basilica of St. Mary Major, President of the Commission of Cardinals
– Cardinal Josip Bozanic, Archbishop of Zagreb
– Cardinal Thomas Christopher Collins, Archbishop of Toronto
– Cardinal Pietro Parolin, Secretary of State
– Cardinal Christoph Schönborn, Archbishop of Wien

– Cardinal Jean-Louis Tauran, President of the Pontifical Council for Interreligious Dialogue.

The **Prelate** is appointed by the Commission of Cardinals. The Prelate:
– Oversees the activities of the Institute and may have access to its acts and documents;
– Participates, as Secretary, in meetings of the Commission of Cardinals, drafting the minutes of the meeting;
– Attends the meetings of the Board of Superintendence;
– Submits his comments to the Commission of Cardinals, notifying the Board of Superintendence.

Msgr. Battista Mario Salvatore Ricca was appointed as the **Prelate** of the Institute in June 2013.

The **Board of Superintendence** is responsible for the administration and management of the Institute, as well as the oversight and supervision of its financial, economic and operational activities. In particular, the Board has the task of:
– Formulating general policy guidelines and basic strategies for the activities of the Institute in line with its mission;
– Defining the criteria for the implementation of annual programs and objectives of the Directorate, and approving its proposals;
– Verifying the economic-financial activities of the Institute;
– Monitoring compliance with established programs and objectives, with regard to investments and other activities;
– Defining the most appropriate financial structure for the Institute, proposing the ways to improve it, and in general, the best means to increase its assets and activities in the context of correct adherence to economic-financial rules and in full compliance with the overall mission of the Institute;
– Proposing to the Commission of Cardinals changes to the Statutes as long as they are unanimously approved by the Board of Superintendence;
– Arranging for the issuance of the Institute's Regulations, which are required to provide a detailed description of the powers and competencies of the Board and of the Directorate;
– Delegating signing power in the name of the Institute to the Director General and, at their request, the Vice-Director, Managers and Officers, in the manner prescribed in the Regulations;
– Approving the Financial Statements prepared by the Directorate.

The members of the Board of Superintendence are nominated by the Commission of Cardinals and serve for a five year term, and can be reappointed.

In 2017 Board of Superintendence comprised:
– Jean-Baptiste Douville de Franssu, President
– Mary Ann Glendon (Until February 2018)
– Michael Hintze
– Mauricio Larraín
– Scott C. Malpass
– Javier Marín Romano
– Georg Freiherr von Boeselager

Cardinal Christoph Schönborn
Archbishop of Wien

Cardinal Jean-Louis Tauran
President of the Pontifical Council for Interreligious Dialogue

PRELATE

Msgr. Battista Mario Salvatore Ricca

IN 2017 BOARD OF SUPERINTENDENCE COMPRISED:

Jean-Baptiste Douville de Franssu, President

Mary Ann Glendon
(Until February 2018)

Michael Hintze

Mauricio Larraín

Scott C. Malpass

Until February 2018, the Board was comprised also of Prof. Mary Ann Glendon, who resigned. The Board wishes to express its gratitude to Mary Ann Glendon for all the help and counsel she provided to the IOR during her tenure.

The **Directorate** is responsible for all operational activities of the Institute and is accountable to the Board of Superintendence.

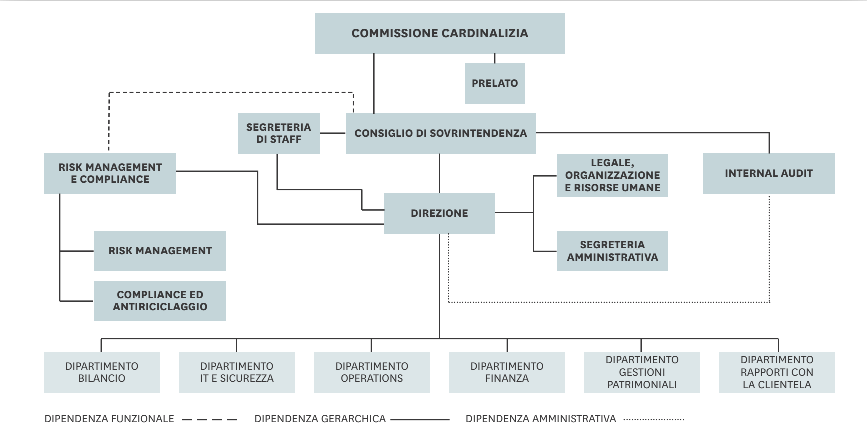
The Directorate is appointed by the Board of Superintendence and approved by the Commission of Cardinals and in 2017 consisted of:
– Gian Franco Mammì, Director General
– Giulio Mattietti "Aggiunto al Direttore" with delegated functions (Until November 2017)

The **Revisori** must:
– Verify at least quarterly, the administrative and accounting review of the Institute's books and records;
– May conduct internal audits or other inspections, if requested by the Board of Superintendence;
– Review the financial statements including the report of the Directorate and supporting documents, provide written comments to the Board of Superintendence and present their observations to the attention of the Directorate and the Prelate.

The *Revisori* are three, appointed by the Board of Superintendence for a maximum period of three years. They can be reappointed.

In 2017 members were:
– Mario M. Busso, President of the *Revisori*
– Giovanni Barbara (until March 2018)
– Luca Del Pico

4. IOR ORGANIZATION CHART



5. CONTROL FUNCTIONS

Since 2015 a focus was made on the development of appropriate **control functions**, reinforcing their independence and ensuring that activities and controls were properly carried out. Today, they are comprised of:

– Internal Audit
– Risk management and Compliance

In accordance with law no. XVIII/2013 (see art. 27 et seq.) and best international practices, the Internal Audit function reports to the Board with a dotted line to the Directorate.

In terms of second-level controls, Risk management and Compliance department is directly responsible, among other things, for the AML/CFT (Anti Money Laundering/Combating the Financing of Terrorism) activities.

6. REGULATORY FRAMEWORK AND TAX REQUIREMENTS

Regulatory framework

The Institute is subject to the laws and regulations of the Holy See and Vatican City State.

The Vatican legal framework recognizes the Canon Law as the primary source of legislation and the primary criterion for its interpretation. Furthermore, there are six organic laws and other ordinary laws specific to the Vatican City State. For matters not covered by Vatican laws, laws and other regulations issued by the Italian Republic are observed as supplementary, subject to prior approval by the competent Vatican authority. They are adopted on the condition that they do not conflict with the doctrine of divine law, the general principles of Canon Law or the provisions of the Lateran Pact and subsequent Agreements, and provided that they are applicable to the state of affairs existing in Vatican City State (See law No LXXI on the source of law, promulgated by Pope Benedict XVI on 1 October 2008).

According to article 1.4 of Law no. LXXI on the sources of law, the legal framework must also conform to the general norms of international law, and to those arising from treaties and other agreements to which the Holy See is part of.

Javier Marín Romano

Georg Freiherr von Boeselager

THE DIRECTORATE IN 2017 CONSISTED OF:

Gian Franco Mammì
Director General

Giulio Mattietti
"Aggiunto al Direttore" with delegated functions
(Until November 2017)

The Institute is subject to Law no. XVIII of 8 October 2013 that covers norms of transparency, supervision, and financial intelligence and, as an entity that carries out financial activities on a professional basis in Vatican City State, it is also subject to Regulation No. 1 "Prudential Supervision of Entities carrying out financial activities on a professional basis" issued by AIF and enacted on 13 January 2015.

The Regulation No. 1, establishing a clear system of authorization, stipulates the criteria for the organization and management of entities and mechanisms of internal control.

On 15 December 2016, the AIF promulgated the "Circular relating to the preparation of the annual financial statements and the consolidated financial statements of entities carrying out financial activities on a professional basis". These financial statements have been prepared in accordance with the aforementioned Circular.

Tax requirements

On 15 October 2016 the "Agreement between the Government of the Italian Republic and the Holy See in tax matters" became effective. In force of the Agreement, the clients resident in Italy for tax purposes fulfill their tax debts, arising from the financial assets held with entities carrying out financial activities on a professional basis in Vatican City State, through a Fiscal Representative chosen by the Institute. The IOR provides the calculations and withholds taxes to customers which are paid to the Italian Government via an Italian Tax Representative.

Effective 2015, the IOR is subject also to the Foreign Account Tax Compliance Act (FATCA), a United States federal law that requires U.S. persons, including individuals who live outside the United States, to report their financial accounts held outside of the United States to the U.S. Internal Revenue Service (IRS).

FATCA also requires foreign financial institutions to report to the IRS the accounts of their U.S. clients. In this context, the Holy See has reached an Intergovernmental agreement (IGA) with the United States signed in June 2015. The IOR has been assigned an identification code (GIIN) by the IRS. The IOR fully complies with the terms of the IGA.

7. PROPOSAL OF DISTRIBUTION OF THE NET PROFIT FOR THE YEAR

For the net profit for the year ended 31 December 2017 amounting to EUR 31.9m, the Board of Superintendence intends to propose to the Commission of Cardinals, that the profits be distributed in full without making any provision to the Reserves, also considering the adequacy of capital (for further details see Part 6 - paragraph 6.2.2 "Capital adequacy").

Chapter 2
Operational information

1. 2017 BUSINESS REVIEW

Macroeconomic environment

2017 was characterized by a synchronized recovery of all the major economies. According to estimates by the International Monetary Fund, at the end of 2017, global GDP will be around 3.6%. For the United States it was the eighth consecutive year of expansion, supported by low interest rates, a labor market that has almost reached full employment and a high degree of confidence of companies and households. The positive economic situation took effect especially in the second half of 2017 and other positive results are expected from investments in infrastructures and the tax reform requested by President Donald Trump. Growth in the Eurozone also improved slightly, progressively extending more evenly to peripheral areas. In this area too, in support of this growth, other factors such as the upturn in international trade, with the growth in consumption, have had a weight, in addition to low interest rates, with the effect of favoring exports and consolidating the investment cycle. Among the emerging countries, Russia and Brazil returned to growth, India is recovering, and higher than expected results were recorded in China.

This general path of development has not slowed down even with potentially destabilizing political events such as tensions between the international community and North Korea, the uncertain outcome of the German parliamentary elections with the consequent difficult governability, as well as the revived separatist tensions in Catalonia. The Asian political situation was instead rather stable, thanks to the victory in Japan of Prime Minister Abe in the October elections, with a consequent extension of the government mandate until 2021 and in China, thanks to the re-confirmation of Xi Jinping at the helm of the Communist Party and of the country's government for a further five years.

2017 marked the beginning of the trend reversal in monetary policy. The set of extraordinary stimuli that allowed the main economies to come out of the crisis after 2008, begins to be gradually reduced, always trying not to compromise growth. The Federal Reserve (FED) has started moderately the path of rising interest rates with three increases during the year, the last in December that brought rates to 1.5%. Starting in October, the FED has also started a program to reduce the reinvestment of maturing debt securities with the aim of gradually reducing its balance sheet. 2017 was also the year of the appointment of Jerome Powell, chosen by Trump to take the helm of the American Central Bank in place of Janet Yellen.

In Europe, the ECB continued to maintain an expansionary monetary policy during the year, given that inflation remained limited and far from the medium-term targets, but nevertheless triggered the start of the program to reduce purchases of securities that will continue gradually also in 2018, in light of an improvement in the macroeconomic scenario. In the United Kingdom, against an acceleration of inflation, the BOE also began a gradual increase in rates. On the contrary, the Bank of Japan continued to pursue a very accommodative economic policy due to inflation very close to zero.

In 2017, volatility was particularly low on the financial markets, which

Gian Franco Mammì
Director General

FINANCIALS 2017

51.3 m Eur
Intermediation margin

19.1 m Eur
Operating costs

31.9 m Eur
Profit for the year

reacted to economic and political uncertainties in a lower tone than what would have been expected by looking at the past experience.

The asset class that performed best in 2017 is undoubtedly equities which reached historical highs in many financial centers. The price lists continued to mark records and the positive results of companies have boosted this trend.

In the United States, during 2017, the acceleration of share prices occurred mainly in the second half of the year and was also supported by the approval of the tax cuts plan by the Trump administration with benefits mainly for companies that, thanks to lower taxation, can benefit from positive effects on their financial statements. The performance of the equity markets was also generally positive in Europe. The increase in prices was supported by good business fundamentals and a high rate of job creation.

However, much lower results are recorded for government bonds. In the US, the rate of return on 10-year Government Bonds was characterized by an initial phase of reduction due to disregarded expectations on tax reforms and below-expected inflation data. In the second half of the year, with the announcement from the FED of a reduction in securities held in the balance sheet as well as continued strong growth, yields rose again, closing the year at 2.42%. On the other hand, yields on the short-term bonds continued to gradually rise, driven directly by monetary policy actions.

The market of European government bonds recorded returns that were substantially stable or slightly up (both on the short and long part of the curve). During the year, the yield on 10-year German Government Bonds rose from 0.21% to 0.43%, and in the same period the yield of Italian Government Bonds with the same maturity rose from 1.81% to 2.02%. The year was nevertheless characterized by low volatility, mainly linked to the monetary policy, with the announcement of the reduction in purchases of securities that produced a strong upward trend in yields in the first part of July, then partially subsided.

On the foreign exchange market, 2017 closed with the Euro significantly increasing in value against the US Dollar. The EUR-USD exchange rate rose from 1.05 to 1.20. The Euro also increased against the Yen, the Swiss Franc and to a lesser extent the Pound. The emerging currencies ended the year with a positive sign, thanks mainly to the weakness that characterized the US Dollar and the improvement of the economic outlook.

2017 was a volatile year for the price of gold, which had to face events such as the Trump settlement, political tensions with North Korea, and the gradual changes in central bank strategies. Coinciding with the recovery of the Dollar in the second half of the year, we witnessed the weakening of gold from the September highs over $ 1,350 to the lows around $ 1,240 at the end of December.

Prospects have improved significantly for oil. The price trend seems to be directed strongly to the upside. The global consumption of crude was solid thanks to the contribution of China and the supply is still destined to contract following the agreements reached by the producing countries. The geopolitical tensions have not strongly influenced the trend.

Composition of the Client base

At the end of 2017, the IOR clients amounted to 14,945 (2016: 14,960) and, measured by assets entrusted, comprised religious orders (52%), Roman Curia departments, Holy See Offices and nunciatures (11%), episcopal conferences, dioceses and parishes (9%) entities of Canon Law (8%), cardinals, bishops and clergy (8%), vatican employees and pensioners (8%), others, included Canon Law foundations (4%).

The IOR's customers have a common characteristic, which is that they are part of and serve the Catholic Church (see client definition in Chapter 1).

To its clients IOR offers the services of acceptance of deposits, asset management, securities custody.

As of 31 December 2017, the net value of assets held in managed portfolios was EUR 3.0bn (2016: EUR 3.1bn), the net value of assets held in non-managed portfolios was EUR 474.6m (2016: EUR 554.8m) and the value of customer deposits was EUR 1.8bn (2016: EUR 2.0bn), resulting in EUR 5.3bn in total client assets (2016: EUR 5.7bn).

(in thousand Euro)

	2017			2016		
	In Balance Sheet	Off Balance Sheet	Total	In Balance Sheet	Off Balance Sheet	Total
Customer deposits (including Legates)	1,839,536		1,839,536	2,028,973		2,028,973
Assets under Custody		474,594	474,594		554,763	554,763
Assets under Management	332,696*	2,624,957	2,957,652	410,563 *	2,700,366	3,110,929
Total	**2,172,232**	**3,099,550**	**5,271,782**	**2,439,536**	**3,255,129**	**5,694,665**

*Deposits of Assets under Management are net of commissions collected in the first days of the subsequent year.

Assets under Custody mainly include client-owned securities held at the IOR for custodial purposes, in accordance with the mission of the Institute. For the purpose of the table above, securities, gold and precious metals under custody are stated at market values.

Assets under Management consist mainly of client-owned securities held at the IOR for management purposes, on the basis of portfolio management mandates, compliant with the mission of the Institute. For the purpose of the table above, securities under management are stated at market values.

Income Statement

In 2017, IOR's Net profit was EUR 31.9m (2016: EUR 36.0 m). The overview of the items that contributed to determine this result shows an improvement of the ordinary activity result of the Institute.

In fact, 2017 accounts were characterized by an increase in trading activities and a reduction in administrative expenses which are partially offset by a reduction in interest income due to the low rates offered by the market. The intermediation margin grew by 16.3% compared to 2016, reaching EUR 51.3m (2016: EUR 44.1m).

Furthermore, in 2017 there is not the extraordinary item that characterized the 2016 financial statements, the release of 13 million of the provision related to tax exposure towards other countries.

A brief overview of the main components of the Income Statement is presented below.

The most significant source of revenues is the profit derived from Treasury activities on proprietary portfolios. The most important component was derived from bond yeld which contributed for EUR 32.0m (interest of EUR 30.5m and trading income EUR 1.5m).

Interest Margin amounting to EUR 29.0m decreased by 21% (2016: EUR

36.7m). This was affected by the decline in the yield on investments in securities and bank deposits, although the average amounts of capital invested remained unchanged at EUR 2.9bn (2016: EUR 2.9bn). The average rate on customer deposits remained unchanged at 0.14% (2016: 0.14%), while the average yield on investments in securities and bank deposits declined to 1.09% (2016: 1.35%). Accordingly, the spread between the average rate received on assets and the average rate paid on liabilities decreased from 1.22% to 0.95%. This was mainly due to the expiration of securities in 2017 purchased in previous years with a nominal interest rate higher than those currently available on market.

Net Income for trading activities recognised a net gain of EUR 7.5m (2016: EUR -9.0m affected by the decrease in UCI unit investment to EUR -12.8m). In 2017 UCI unit investment lost EUR -700,000.

The improvement in the results was also due to the positive performance of the equities held in the proprietary portfolio compared to 2016.

Stable was the contribution to the result from debt securities. They recognised a positive total net profit, including gains and losses from trading and gains and losses from valuation, amounting to EUR 1.5m in 2017 (2016: EUR 1.6m). In the actual market scenario such stability was not assured and it is a positive consequence of the positive reaction of proprietary portfolio to market trends during the year.

Finally, Forex activity accounted for income of EUR 3.2m (2016: EUR 2.0m).

Dividends decreased by 47.6% to EUR 1.1m (2016: EUR 2.1m).

Net Fee and Commission income decreased 3.9% to EUR 12.3m in 2017 (2016: EUR 12.8m). Fee and Commission Income increased by 0.6%, to EUR 15.9m in 2017 from EUR 15.8m in 2016. In fact, the reason of the decrease in the margin is the increase of Commission Expense from EUR 3.0m in 2016 to EUR 3.6m in 2017 (+20%).

The most important element of the Fee and Commission Income was commissions from Asset Management services, which reached EUR 12.5m, the same result as 2016. The slight growth in Commission Income is due to commissions on trading in financial instruments, increased in 2017 to EUR 711,000 (2016: EUR 654,000) due to the increase in customer transactions.

The increase in Fee and Commission Expense was mainly due to the fees paid for bank deposits which increased to EUR 1.4m in 2017 (2016: EUR 571,000), recording +145% as increase.

Administrative Expenses were EUR 18.7m in 2017 (2016: EUR 19.1m). This includes Staff Expenses of EUR 11.4m in 2017, increased from the prior year amount (2016: EUR 10.2m, or +11.8%).

Administrative expenses also include expenses for professional services, which decreased in 2017 reaching EUR 2.7m (2016: EUR 4.0m). This was due to lower extraordinary costs incurred during the year from the completion of certain projects.

Other administrative expenses decreased by 6.1% to EUR 4.6m in 2017 (2016: EUR 4.9m) due to the review of outstanding contracts.

Other Operating Income (Expense) recognised income of EUR 164,000 (2016: income of EUR 7,000).

Balance Sheet

As of 31 December 2017, total assets on the IOR's balance sheet were EUR 3.0bn (2016: EUR 3.3bn), with equity of EUR 659.1m (2016: EUR 672.6m).

On the Liabilities side, **Due to customers** is the most significant line item, representing 71.1% of total liabilities. The balance decreased from the prior year, amounting to EUR 2.1bn (-12.5%). Customer deposits decreased by EUR 189.4m and asset management liquidity decreased by EUR 78.1m. This was due to Forex effect on US Dollars deposits and to tax payments on financial instruments made through the Institute.

As previously reported in Chapter 1, credit activity is residual and strictly subject to constraints of the internal policies as established by the Board of Superintendence.

The Asset side of the Balance Sheet mainly reflects bank deposits and securities, and less than 3% of total assets is held in UCI units and equities.

Bank Deposits totaled EUR 473.4m at the end of 2017 (2016: EUR 643.2m). These mainly consisted of EUR 362.1m in deposits on demand (2016: EUR 457.6m), and EUR 54.2m in term deposits in the interbank lending market (2016: EUR 108.5m). The remaining part, EUR 57.1m (2016: EUR 77.1), concerned term deposits with APSA.

The value of IOR **Securities** (debt securities, equity securities and investment funds) was EUR 2.4bn in 2017 (2016: EUR 2.5bn).

Bonds, at EUR 2.3bn, were the most significant investments, representing 97.2% of the securities held as of 31 December 2017, while equities accounted for 1.4%, and investment funds for 1.4%. As previously explained, the volume of the securities in the portfolio slightly decreased compared to 2016, while the portfolio composition remained unchanged. The decrease was mainly recorded in the "financial assets held to maturity" portfolio due to the expiration of some securities and in the absence of purchases made in 2017 in the same portfolio.

Profitability ratios

The table below highlights the main economical, financial and productivity ratios:

Profitability ratios (%)	2017	2016
ROE (Return on Equity)	5.1%	5.7%
ROA (Return on Assets)	1.1%	1.1%
Operating costs / Intermediation margin	37.3%	15.5%
Interest margin / Intermediation margin	56.4%	83.1%
Net fee and commission income / Intermediation margin	24.0%	29.0%
Interest margin / Total Assets	1.0%	1.1%
Intermediation margin / Total Assets	1.7%	1.3%
Core Equity TIER 1	68.3%	64.5%

While ROA was in line with the previous year, ROE recorded a slight decrease compared with the previous year due to the decrease in Net profit.

The profitability, explained from the ratio "interest margin / total assets", amounted in 2017 to 1.0% against 1.1% recorded in 2016, due to the reduction of interest margin; instead, the other profitability index, calculated as the ratio between the intermediation margin and total assets, recorded a relevant increase thanks to lower write-downs of UCI units in portfolio and the higher contribution of the equity shares (1.7% in 2017 compared to 1.3% in 2016).

These two ratios showed that the Institute ability to create income increased. The increase in the operating costs / intermediation margin ratio is not a real increase because the index in 2016 was affected by the reestimation of tax provision for exposure in foreing countries (EUR 13m).

Other aspects

The IOR does not issue securities or underwrite or place securities; it protects its client assets by primarily investing in financial instruments characterized as very low risk (e.g. government bonds, bonds issued by institutions and international organizations, as well as deposits in the interbank market).

The IOR has no branches and provides services only at the IOR office located in the Vatican City State.

The Institute is the single shareholder of the real estate company Società per Gestione di Immobili Roma (S.G.I.R. S.r.l.), which is governed by Italian law and takes the legal form of a limited liability company, with its registered office in Rome, which it was specifically set up to more easily and transparently manage the owned real estate located in Italy.

2. PREVALENCE OF CATHOLIC PRINCIPLES AND VALUES IN THE MANAGEMENT OF PROPRIETARY AND CUSTOMERS' FINANCIAL ASSETS

Undertaking the commitment to remain faithful and give concreteness to the words pronounced by the Holy Father Francis during his speech to the members of the Board of Superintendence in November 2015: "The main goal of the IOR cannot be to have the maximum possible gain, but should be goals that are compatible with the norms of morality, consistent efficiency and practices respecting the specificity of its nature and exemplarity in its mode of operation", in 2017, the IOR continued to responsibly manage its financial resources, and those entrusted to it, in accordance with the Catholic principles and values that inspire it.

Catholic principles and values are non-negotiable and cannot be based on the logic of expected return.

Therefore, also in 2017, while seeking to pursue a return on its investments that is, to the extent possible, in line with that of the referenced market, the Institute continued to favour the consistency of these investments with the Catholic principles and values by which it is guided in its work.

Ethical investments

The glorification of human life, creation and human dignity are some of the inalienable values that guided the Institute in the selection of the investments made in 2017.

Indeed, the Institute expressed its commitment to contribute to the "care of the common home", invoked by Pope Francis in the Encyclical Letter *Laudato si'*, and selected its investments also on the basis of two fundamental themes recalled by the Holy Father:

a) corporate social responsibility; and

b) the role of companies in creating a sustainable future.

In 2017, the Institute continued to rule out investments in companies that violate or do not fully respect the globally recognized principles of human rights, labour standards, the fight against corruption and the fight against environmental crime. The Institute also expressed its willingness to give up investments already under way if compliance with these principles by the selected companies ceased to exist due to force majeure, subsequently occurred in the geo-political context of reference.

The Institute continued also to invest in projects to promoting the development of poorer countries with choices consistent with the realization of a sustainable future for future generations.

3. CHARITABLE AND SOCIAL ACTIVITIES

In addition to the transfer of the annual profit of the 2016 financial statements, which has been placed in full availability of the Holy Father, in 2017, the Institute for Works of Religion has contributed to the realization of numerous charitable and social activities through:

a. donations intended to respond to requests for aid or contributions received by the Institute. In the year under review, the most common ones were the direct disbursement of contributions to student priests for the completion of university studies, financial aid for destitute persons or families (reported by Parishes or by individual priests), long-distance adoptions, specific help for missionary and charity work, aid to families that have lost everything as a result of natural disasters, etc., and
b. the granting of properties owned by the Institute - located within the Italian territory - for rent with subsidized rent or on loan for free use to support institutions with a social purpose.

The decisions concerning the recipients and the amount of donations referred to in point a) above are always collegial and have been adopted by the Charity Committee - chaired by the Prelate and composed of managers and employees of the Institute - or directly by the Commission of Cardinals.

On the other hand, with regard to the granting of properties referred to in point b), the Institute relies on S.G.I.R. S.r.l., a limited liability company under Italian law, of which the Institute is sole shareholder, specifically established, as already disclosed, to manage its own properties in a transparent and more effective manner, which have been received in the course of its history in the form of donations or legacies by institutions and individuals, located in the Italian territory.

Alongside the typical activities of a real estate company, the forms of management used by S.G.I.R. S.r.l. also include the granting of properties:

1. *For rent with subsidized leases*, to help associations or other Catholic institutions that, due to their fragile budgets, could not afford to rent to market;
2. *On loan for free use*, in favour of structures that offer hospitality and support to people in conditions of particular fragility or risk, such as young single mothers or victims of violence, refugees, the sick and the needy.

4. FORECAST FOR 2018

In the first months of 2018, the Institute's activity was in line with the Strategic Plan approved by the Board of Superintendence in January 2017. The main objective is to improve the quality of services offered to clients and the inflows of customer deposits. By the end of 2018, the results of this work should be fully apparent.

The IOR will continue to operate in accordance with its Mission that is to serve the Holy Father with prudence, in His mission as the Universal Pastor, through the provision of dedicated financial advisory, in complete compliance with Vatican and international laws in force.

IOR Istituto per le Opere di Religione

Financial Statement

BALANCE SHEET

(in Euro)

ASSETS	2017	2016
10 Cash and cash equivalents	71,233,924	50,850,340
20 Financial assets held for trading	2,116,770,781	1,918,104,346
40 Financial assets available for sale	4,571,559	6,664,406
50 Financial assets held to maturity	246,167,943	558,955,610
60 Due from banks	473,386,281	643,229,012
70 Due from customers	25,422,935	29,152,785
100 Investment in subsidiaries	15,834,950	15,834,950
110 Tangible assets	3,246,863	3,095,565
120 Intangible assets	870,593	1,043,850
150 Other assets	41,502,287	41,958,806
Total Assets	**2,999,008,116**	**3,268,889,670**

(in Euro)

LIABILITIES AND EQUITY	2017	2016
10 Due to banks	4,096,356	-
20 Due to customers	2,131,421,457	2,398,924,457
100 Legates	47,035,020	47,074,644
110 Other liabilities	15,611,737	18,709,825
120 Staff severance fund	7,177,320	6,992,585
130 Provision for risks and charges	**134,547,342**	**124,588,179**
(a) Provisions for pensions and similar obligations	133,335,156	121,088,179
(b) Other provisions	1,212,186	3,500,000
140 Valuation reserves	(54,948,816)	(45,534,851)
160 Reserves	**382,134,172**	**382,134,172**
(a) Unavailable reserves	100,000,000	100,000,000
(b) Available reserves	282,134,172	282,134,172
170 Capital	300,000,000	300,000,000
180 Net profit for the year	31,933,528	36,000,659
Total Liabilities and Equity	**2,999,008,116**	**3,268,889,670**

INCOME STATEMENT

(in Euro)

INCOME STATEMENT	2017	2016
10 Interest and similar income	32,162,670	39,831,730
20 Interest and similar expense	(3,200,984)	(3,168,836)
30 Interest margin	**28,961,686**	**36,662,894**
40 Fee and commission income	15,927,102	15,836,850
50 Fee and commission expense	(3,622,674)	(3,029,222)
60 Net fee and commission income	**12,304,428**	**12,807,628**
70 Dividends and similar income	1,145,494	2,107,013
80 Net income for trading activities	7,526,946	(8,982,924)
100 Profit (loss) on disposal or repurchase of:	**1,386,221**	**1,499,109**
(b) Financial assets available for sale	1,386,221	1,499,109
120 Intermediation margin	**51,324,775**	**44,093,720**
130 Net losses/reversal on impairment:	**(392,122)**	**(1,331,864)**
(a) Receivables	(392,122)	(1,045,306)
(b) Financial assets available for sale		(148,314)
(d) Other financial operations		(138,244)
140 Net income from financial operations	**50,932,653**	**42,761,856**
150 Administrative expenses:	(18,727,173)	(19,085,562)
(a) Staff expenses	(11,441,178)	(10,244,959)
(b) Professional services expenses	(2,655,023)	(3,961,573)
(c) Other administrative expenses	(4,630,972)	(4,879,030)
160 Net provisions to risks and charges		13,000,000
170 Net value adjustments to/recoveries on tangible assets	(68,818)	(82,789)
180 Net value adjustments to/recoveries on intangible assets	(488,981)	(682,777)
190 Other operating income (expense)	163,724	7,287
200 Operating costs	**(19,121,248)**	**(6,843,841)**
220 Net result of fair value valuation of tangible and intangible assets	122,123	82,644
250 Profit (loss) from current operations before taxes	**31,933,528**	**36,000,659**
270 Profit (loss) from current operations after taxes	**31,933,528**	**36,000,659**
290 Profit (loss) for the year	**31,933,528**	**36,000,659**

STATEMENT OF COMPREHENSIVE INCOME

(in Euro)

	2017	2016
10. Profit (loss) for the year	**31,933,528**	**36,000,659**
Items that will not be reclassified to Income Statement		
40. Defined benefit plans	(11,076,131)	(13,275,014)
Items that are or may be reclassified to Income Statement		
100. Financial assets available for sale	1,662,166	(4,278,583)
130. Total other income items	**(9,413,965)**	**(17,553,597)**
Comprehensive income (item 10 + item 130)	**22,519,563**	**18,447,062**

STATEMENT OF CHANGES IN EQUITY

(in Euro)

2017				**Allocation of previous year profit**		**Changes during the year**			
	Total net equity at 31,12,2016	**Changes in opening balances**	**Total net equity at 01,01,2017**	**Reserves**	**Dividends and other allocations**	**Changes in reserves**	**Extra dividend distribution**	**Comprehensive income 2017**	**Net Equity at 31,12,2017**
Capital	300,000,000		300,000,000						300,000,000
Reserves									
(a) unavailable	100,000,000		100,000,000						100,000,000
(b) available	282,134,172		282,134,172						282,134,172
(c) other									
Valuation reserves	(45,534,851)		(45,534,851)					(9,413,965)	(54,948,816)
Net profit (loss) for the year	36,000,659		36,000,659		(36,000,659)			31,933,528	31,933,528
Net Equity	672,599,980		672,599,980		(36,000,659)			22,519,563	659,118,884

2016				**Allocation of previous year profit**		**Changes during the year**			
	Total net equity at 31,12,2015	**Changes in opening balances**	**Total net equity at 01,01,2016**	**Reserves**	**Dividends and other allocations**	**Changes in reserves**	**Extra dividend distribution**	**Comprehensive income 2016**	**Net Equity at 31,12,2016**
Capital	300,000,000		300,000,000						300,000,000
Reserves									
(a) unavailable	100,000,000		100,000,000						100,000,000
(b) available	282,134,172		282,134,172						282,134,172
(c) other									
Valuation reserves	(27,981,254)		(27,981,254)					(17,553,597)	(45,534,851)
Net profit (loss) for the year	16,126,935		16,126,935		(16,126,935)			36,000,659	36,000,659
Net Equity	670,279,853		670,279,853		(16,126,935)			18,447,062	672,599,980

CASH FLOW STATEMENT

(in Euro)

DIRECT METHOD	2017	2016
A. Operating activities		
1. Management	**39,121,105**	**42,833,712**
Interest income	38,153,573	48,639,880
Interest expense	(3,153,835)	(3,168,341)
Dividends and similar income	1,145,494	2,107,013
Net commissions	12,304,428	12,807,628
Realised profit (loss) from trading activities	7,879,311	2,024,715
Staff expenses	(10,085,597)	(10,566,173)
Other administrative expenses	(7,285,995)	(8,840,603)
Other income (expense)	(163,726)	(170,407)
2. Cash generated by/(used in) financial assets	**(21,108,946)**	**(206,618,819)**
Financial assets held for trading	(199,939,285)	(266,429,528)
Financial assets available for sale	5,141,233	5,575,219
Due from banks: on demand	95,500,207	(192,197,353)
Due from banks: other receivables	74,301,718	192,249,112
Due from customers	3,430,661	54,408,236
Other assets	456,519	(224,505)
3. Cash generated by/(used in) financial liabilities	**(268,879,319)**	**62,216,802**
Due to banks: on demand	4,096,356	(10,591,428)
Due to banks: other payables		
Due from customers	(267,550,149)	75,515,176
Outstanding securities		
Legates	(39,624)	(1,191,659)
Financial liabilities held for trading		
Financial liabilities carried at fair value		
Other liabilities	(5,385,902)	(1,515,287)
Cash generated by/(used in) operating activities	**(250,867,160)**	**(101,568,305)**
B. Investing activities		
1. Cash generated by:	**308,161,037**	**53,250,000**
Disposals of investments in subsidiaries		
Dividends received on investments in subsidiaries		
Disposal/reimbursement of financial assets held to maturity	308,161,037	53,250,000
Disposals of tangible assets		
Disposals of intangible assets		
2. Cash used in:	**(413,717)**	**(965,804)**
Purchases of investments in subsidiaries		
Purchases of financial assets held to maturity		
Purchases of tangible assets	(97,993)	(113,986)
Purchases of intangible assets	(315,724)	(851,818)
Cash generated by/(used in) investing activities	**307,747,320**	**52,284,196**
C. Financing activities		
Issues/purchases of capital instrument		
Dividend distribution and other purposes	(36,000,659)	(16,126,935)
Cash generated by/(used in) financing activities	**(36,000,659)**	**(16,126,935)**
Cash generated/(used) during the year	**20,879,501**	**(65,411,044)**

Items	2017	2016
Cash and cash equivalents at beginning of the period	50,850,340	114,737,182
Cash generated/(used) during the year	20,879,501	(65,411,044)
Cash and cash equivalents: forex effect	(495,916)	1,524,202
Cash and cash equivalents at end of the period	71,233,925	50,850,340

Explanatory Notes

PART 1. ACCOUNTING POLICIES

1.1 General information

1.1.1 Statement of compliance with accounting standards

The 2017 financial statement have been prepared in accordance with the Circular concerning the annual financial statements and the consolidated financial statements of entities carrying out financial activities on a professional basis, issued by Authority of Financial Information on 15 December 2016.

As stated in the Circular, the financial statements must be prepared in accordance with the "International Accounting Standards – IAS", the "International Financial Reporting Standards – IFRS" and related Interpretations ("Interpretations SIC / IFRIC"), as adopted by the Vatican in a special arrangement to the Monetary Convention between the European Union and the State of the Vatican City on 17 December 2009.

1.1.2 Accounting policies

The financial statements consist of the Balance Sheet, the Income Statement, the Statement of Comprehensive Income, the Cash Flow Statement, the Statement of Changes in Equity and the Explanatory Notes.

Disclosures under IFRS 7 "Financial Instruments, disclosures" about the nature and extent of risks have been included in Part V "Information on Risks and Hedging Policies".

The accounting principles and valuation methods applied in the preparation of these financial statements, detailed below, are consistent with those of the previous financial year, except for new standards, new interpretations, or amendments of standards.

The financial statements of the Institute are prepared in Euro, while the explanatory notes are expressed in thousand Euro.

For the various items, the 2017 figures and corresponding values for the previous year are provided.

Where necessary, the comparative figures have been adjusted to conform to changes in presentations in the current year.

The financial statements are prepared in Italian.

The financial statements of the IOR were prepared on a going concern basis in accordance with IAS 1 "Presentation of Financial Statements". As of the date of the approval of the financial statements, there were no material uncertainties and therefore no significant doubt regarding the Institute's ability to continue as a going concern in the foreseeable future.

The financial statements fairly present the financial position, financial performance and cash flows of the Institute.

The preparation of the financial statements requires the Directorate to make certain estimates and assumptions about the future where actual results may differ. Estimates and assumptions affect the reported amounts of certain assets, liabilities, revenues and expenses in the financial statements. In addition, changes in assumptions may have a significant impact on the financial statements in the year in which the assumptions change.

The preparation of the financial statements also requires the Directorate to exercise judgements in applying the IOR's accounting policies to estimate the carrying value of assets and liabilities not readily obtainable from other sources.

The Directorate believes that the underlying assumptions are appropriate and that the IOR's financial statements fairly present its financial positions and results. All estimates are based on historical experience and/or expectations with regard to future events that seem reasonable on the basis of information known at the time of the estimate. They are also reassessed on a regular basis and the effects of any variation are immediately reflected in the financial statements.

Those areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Section 1.1.4 "Critical accounting estimates and judgements".

The financial statements do not reflect a provision for taxes because there is no corporate income tax in the Vatican City State.

For the year ended 31 December 2017, the Institute, given the immaterial value of its subsidiary, did not prepare consolidated financial statements in accordance with the provisions of the Conceptual Framework (QC6 – QC11) of IAS/IFRS, since the additional information coming from the consolidated financial statements would be of little relevance for the users of the financial statements.

The Institute provides the additional information required by IFRS 12 "Disclosure of interests in other entities" in Part 5, Section 5.2.6 "Disclosure of unconsolidated structured entities for accounting purposes".

The financial statements of the Institute are prepared by the Directorate and approved by the Board of Superintendence, which will be submitted to the Commission of Cardinals.

The Commission of Cardinals acknowledges the financial statements and decides on the distribution of profits, after taking into account the IOR's own financing needs.

1.1.3 Subsequent events

According the provisions of IAS 10, all events that took place subsequent to 31 December 2017 have been evaluated in the preparation of the 2017 Financial Statements.

1.1.4 Critical accounting estimates and judgements

Critical judgements in applying the Institute accounting policies

In the process of applying the accounting policies adopted by IOR, which are described in Section II, there may be circumstances that lead the Directorate to make judgements that have a significant impact on the amounts recognized in the financial statements.

Such circumstances and related judgements may be part of the valuation process used for financial instruments. The Directorate makes critical judgements when deciding the asset category for classification, determining whether a market is active or not, whether the asset is liquid or illiquid, market inputs and parameters to be used, when they must be reviewed, and assessing circumstances where internal parameters are more reliable than market-based ones.

Retirement benefits and other post-employment liabilities are estimated trough an actuarial valuation performed by an independent expert. Such an evaluation is based on critical judgements because estimates are made about the likelihood of future events and the actual results could differ from those estimates.

Estimates that contain elements of uncertainty

The process of applying the IOR's accounting policies may require the use of key assumptions affecting the future, and/or other sources of estimation uncertainty as of the balance sheet date, with a significant risk of causing material adjustments to the carrying amount of assets and liabilities in the next financial year.

Key assumptions and judgments made in the 2017 Financial Statements relate to the assessment of illiquid debt securities held for trading and external investment funds included within the portfolio held for trading, as disclosed in the section 1.4 "Fair value information".

Illiquid securities are not quoted in active markets and their fair value is not readily available in the market. These securities subject to estimation uncertainties (Level 3 of fair value hierarchy) amounted to EUR 22.3m as of 31 December 2017 (2016: EUR 23.3m). These were exclusively comprised of externally managed investment funds.

With reference to the contingent liabilities related to commitments linked to externally managed investment funds, they are valued taking into account all available information at the date of preparation of these financial statements. The dispute in progress is currently at an early stage so there are no significant information to be highlighted in the financial statements.

This assessment is made on the basis of assumptions and the process of estimation is characterized by elements of uncertainty. By their nature, the estimates and assumptions used may vary from one period to another and, therefore, it can not be excluded that in subsequent periods the amounts of such liabilities may differ materially from those currently estimated as a result of new information and charges in the evaluations made.

In past years, the IOR has worked to review and confirm its tax position and that of its clients in countries where investment relationships exist. This review has identified probable contingencies related to prior years as a result of different interpretations regarding the legal nature of the Institute and the related applicable tax treatments.

During 2017, the IOR has almost reached the final estimate of the outstanding liability and has made the expected tax payments. Pending the formal and definitive conclusion of this issue, IOR has maintained on its books a residual provision of EUR 1.2m, included in the Balance Sheet, item liability of 130 "Provision for risks and charges" line b "Other provisions". As this represents an estimate based on critical assumptions, upon the conclusion of future events, actual results may differ from what is expected.

1.1.5 Impact of New Accounting Pronouncements

Accounting standards, amendments and interpretations IFRS effective 1 January 2017

The following accounting standards, amendments and interpretations IFRS were adopted for the first time by the IOR effective 1 January 2017:

- Amendments to **IAS 7 "Disclosure Initiative"** (published on 29 January 2016). The document aims to provide some clarification to improve disclosures about financial liabilities. In particular, the amendments required to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities. The adoption of the amendments had no impact on the disclosures or the amounts recognized in the Institute's financial statements.
- Amendments to **IAS 12 "Recognition of Deferred Tax Assets for Unrealised Losses"** (published on 19 January 2016). The amendment aims to provide some clarifications on the recognition of deferred tax assets on unrealized losses in the valuation of financial assets of the "afs" category upon the occurrence of certain circumstances and on the estimate of taxable income for future years. The adoption of the amendments had no impact on the disclosures or the amounts recognized in the Institute's financial statements.

Accounting standards, amendments and interpretations IFRS and IFRIC approved by the European Union, not yet mandatorily applicable and not early adopted by the Institute at 31 December 2017

- Standard **IFRS 15 – *Revenue from Contracts with Customers*** (published on 28 May 2014 and amended on 12th April 2016) will replace the following standards and interpretations: IAS 18 – *Revenue* IAS 11 – *Construction Contracts*, IFRIC 13 – *Customer Loyalty Programmes*, IFRIC 15 – *Agreements for the Construction of Real Estate*, IFRIC 18 – *Transfers of Assets from Customers*SIC 31 – *Revenues-Barter Transactions Involving Advertising Services*. The standard establishes a new revenue recognition model, which will apply to all contracts with customers except those that fall within the scope of other IAS / IFRS standards such as leasing, the insurance contracts and financial instruments. This core principle is delivered in a five-step model framework:
  - Identify the contract(s) with a customer;
  - Identify the performance obligations in the contract;
  - Determine the transaction price;
  - Allocate the transaction price to the performance obligations in the contract;
  - Recognize revenue when (or as) the entity satisfies a performance obligation.

  The standard is effective for annual reporting periods beginning on or after 1 January 2018. Earlier application is permitted. However, the amendments to IFRS 15, *Clarifications to IFRS 15 - Revenue from Contracts with Customers*, published by the IASB on 12 April 2016, have not yet been endorsed by the European Union. The adoption of the statement has no important impact on the disclosure or on the amounts recognized in the Institute's financial statements.

- Final version of **IFRS 9** - ***Financial Instruments*** (published on 24 July 2014). The document recognized the results of the IASB project to replace IAS 39:
  - Introducing new criteria for the classification and measurement of financial assets and liabilities;
  - With reference to the impairment model, the new standard requires that the estimate of credit losses is carried out on the basis of the expected losses model (and not on the incurred losses model used by IAS 39) using reasonable and supportable information about past events, current conditions and reasonable and supportable forecasts of future economic conditions;
  - Introducing a new hedge accounting model (types of transactions eligible for hedge accounting, changes in the method of accounting for forward contracts and options when included in a hedge relationship, changes in the effectiveness test).

  The new standard is effective for financial statements beginning on 1 January 2018 or later.

  Below is a brief description of the main decisions, choices and activities carried out by the Institute regarding the provisions of the new standard. Regarding the business models identified by the Institute, loans and securities Held to Maturity are classified in accordance with the Held To Collect business model, while the other financial portfolios are classified in accordance with the Held to Collect and Sell or Other (fair value through profit and loss) business models. On 1 January 2018, one of the securities held in the portfolio classified as Available for Sale was reclassified to the portfolio Other (fair value through profit and loss).

  The main impacts expected from the adoption of the new standard are attributable to the application of the new impairment model and, in particular, to the estimate of the "lifetime" expected loss on the credit exposures allocated in stage 2 as well as the collective recognition of impairment of loans to banks. Based on the analysis carried out and the implementations currently in progress, upon adoption, the effects on Common Equity are, under no circumstances, critical in relation to the Institute's solvency profile. Conversely, we note a slight positive impact on Tier 1 capital of 0.1%.

- Standard **IFRS 16 – *Leases*** (published on 13 January 2016), will replace the following standards and interpretations: IAS 17 – *Leases*, IFRIC 4 *Determining whether an Arrangement contains a Lease*, SIC-15 *Operating Leases—Incentives,* SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

  The standard is effective for annual reporting periods beginning on or after 1 January 2019.

  IFRS 16 establishes principles for the recognition, measurement, presentation and disclosure of leases, with the objective of ensuring that lessees and lessors provide relevant information that faithfully represents those transactions. This new standard brings most leases on-balance sheet for lessees under a single model, eliminating the distinction between operating and finance leases. Lessor accounting, however, remains largely unchanged and the distinction between operating and finance leases is retained. The Institute does not expect a significant impact in the financial statements from the application of this standard.

- Document **"*Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts*"** (published on 12 September 2016). For entities whose predominant activity is issuing contracts within the scope of IFRS 4, the document is intended to clarify the concerns arising from the application of the new IFRS 9, starting from January 1 2018, to financial assets. No impact in the financial statements from the application of this document.

Accounting standards, IFRS amendments and interpretations not yet endorsed by the European Union.

At the date of these financial statements, the relevant European Union bodies have not yet completed the approval process necessary for the adoption of amendments and the principles described below.

- Standard **IFRS 17 – *Insurance Contracts*** (published on 18 May 2017), will replace IFRS 4 - Insurance Contracts. The aim of new standard is to ensure that an entity provides relevant information that faithfully represents the rights and obligations arising from the insurance contracts issued. The IASB has developed the standard to eliminate inconsistencies and weaknesses in existing accounting policies by providing a single principle-based framework regarding all types of insurance contracts, including reinsurance contracts that an insurer holds.
  The new standard also provides the disclosure requirements to improve comparability between entities belonging to this sector.
  The new standard measures an insurance contract based on a General Model or a simplified version of this, called the Premium Allocation Approach ("PAA").
  The main features of the General Model are:
  - the estimates and assumptions of future cash flows are always the current ones;
  - the measurement reflects the time value of money;
  - estimates provide for an extensive use of information observable on the market;
  - there is a current and explicit measurement of the risk;
  - the expected profit is deferred and aggregated in groups of insurance contracts at the time of initial recognition; and,
  - the expected profit is recorded in the contractual coverage period taking into account the adjustments deriving from changes in the assumptions related to the cash flows relating to each group of contracts.

  The PAA approach measures the liability for the residual coverage of a group of insurance contracts provided that, upon initial recognition, the entity anticipates that such liability is reasonably an approximation of the General Model. Contracts with a coverage period of one year or less are automatically eligible for the PAA approach. The simplifications deriving from the application of the PAA method do not apply to the assessment of liabilities for existing claims, which are measured with the General Model. However, it is not necessary to discount those cash flows if it is expected that the balance to be paid or collected will take place within one year from the date on which the claim occurred.

  The entity must apply the new standard to insurance contracts issued, including reinsurance contracts issued, to reinsurance contracts held and also to investment contracts with a discretionary participation feature (DPF). The standard is effective from 1 January 2021. Earlier adoption is permitted only for entities that apply IFRS 9 - Financial Instruments and IFRS 15 - Revenue from Contracts with Customers. No impact in the financial statements from the application of this document.

- Amendments to **IFRS 2 *"Classification and measurement of share-based payment transactions"*** (published on 20 June 2016). These amendments clarify the recognition of the effects of vesting conditions in the presence of cash-settled share-based payments, the classification of share-based payments with net settlement characteristics and the booking of changes to the terms and conditions of a share-based payment that modify the classification from cash-settled to equity-settled. The amendments are effective from 1 January 2019, earlier adoption is permitted. No impact in the financial statements from the application of this document.

- Amendments to **IFRS 9 *"Prepayment Features with Negative Compensation"*** (published on 12 October 2017). These amendments specify that a debt instrument with an early redemption option could comply with the characteristics of the contractual cash flows ("SPPI" test) and, consequently, could be measured using the amortized cost method or the fair value through other comprehensive income even if the "reasonable additional compensation" expected in case of early repayment is a "negative compensation" for the lender. The amendments are effective from 1 January 2019, however earlier adoption is permitted. The adoption of the IFRS 9 could have an impact on the SPPI Test on certain securities. No impact in the financial statements from the application of this document.

- Document ***"Annual Improvements to IFRSs: 2014-2016 Cycle"***, published on 8 December 2016, provides partial integration on existing standards, that include:
- IFRS 1 First-Time Adoption of International Financial Reporting Standards - Deletion of short-term exemptions for first-time adopters;
- IAS 28 Investments in Associates and Joint Ventures –

Measuring investees at fair value through profit or loss: an investment-by-investment choice or a consistent policy choice;

- IFRS 12 Disclosure of Interests in Other Entities – Clarification of the scope of the Standard.

The adoption of the above improvement would not affect significantly the Financial Statements.

- Document "***Annual Improvements to IFRSs: 2015-2017 Cycle***", published on 12 December 2017, provides partial integration on existing standards, that include:
  - IFRS 3 *Business Combinations* and IFRS 11 *Joint Arrangements*: the amendment clarifies that when an entity obtains control of a business that represents a joint operation, it must remeasure the interest previously held in that business. However, this process is not envisaged if joint control is obtained,
  - IAS 12 *Income taxes*: the amendment clarifies that all the fiscal effects related to dividends (including payments on financial instruments classified within shareholders' equity) should be accounted for in a manner consistent with the transaction that generated these profits (income statement, OCI or equity),
  - IAS 23 *Borrowing costs*: the amendment clarifies that in the case of loans that remain in place even after the reference qualifying asset is ready for use or for sale, these become part of the totality of the loans used to calculate the financing costs.

  The amendments is effective from 1 January 2019, but early application is permitted. No impact in the financial statements from the application of this document.

- Interpretation **IFRIC 22** "***Foreign Currency Transactions and Advance Consideration***" (published on 8 December 2016). The interpretation clarifies the accounting for transactions that include the receipt or payment of advance consideration in a foreign currency. This document provides guidance on how an entity should determine the date of a transaction, and consequently, the exchange rate to use in circumstances in which consideration is received or paid in advance of the recognition of the related asset, expense or income. IFRIC 22 is effective from 1 January 2018. Earlier adoption is permitted. No impact in the financial statements from the application of this interpretation.

- Interpretation **IFRIC 23** "***Uncertainty over Income Tax Treatments***" (published on 7 June 2017). The interpretation states that the financial statement has to reflect the uncertainties in determining liabilities or assets for taxes only when it is probable that the entity will pay or recover the amount in question. Furthermore, the document does not contain any new disclosure obligation. The interpretation underlines that the entity will have to establish whether it will be necessary to provide information on the comments made by management related to the uncertainty of taxes accounting, in accordance with IAS 1. The new interpretation is effective from 1 January 2019, but early application is permitted. No impact in the financial statements from the application of this interpretation.

- Amendments to **IAS 28** "***Long-term Interests in Associates and Joint Ventures***" (published on 12 October 2017). These amendments clarify the need to apply IFRS 9, including the requirements related to impairment, to other long-term interests in associates and joint ventures for which the equity method is not applied. The amendments are effective from January 1, 2019, but early application is permitted. No impact in the financial statements from the application of this document.

- Amendments to **IAS 40** "***Transfers of Investment Property***" (published on 8 December 2016). These amendments clarify the transfer of a property to, or from, investment property. In particular, an entity shall reclassify a property to, or from, investment property only when there is evidence that there has been a change in use of the property. Such a change must be attributed to a specific event; a change of management's intentions for the use of a property by itself does not constitute evidence of a change in use. The amendments are effective from 1 January 2018. Earlier adoption is permitted. The Institute considers that the application of the above amendments would not affect significantly the Financial Statements.

- Amendments to **IFRS 10 and IAS 28** "***Sales or Contribution of Assets between an Investor and its Associate or Joint Venture***" (published on 11 September 2014). The amendments address a conflict between the requirements of IAS 28 'Investments in Associates and Joint Ventures' and IFRS 10 'Consolidated Financial Statements' and clarify that in a transaction involving an associate or joint venture the extent of gain or loss recognition depends on whether the assets sold or contributed constitute a business. At this stage, the IASB suspended the application of these amendments.

1.2 Information on the main financial statement items

1.2.1 Financial assets held for trading

A financial asset is classified under this category if acquired principally for the purpose of trading.

Purchases of financial assets held for trading are recognized at the transaction date, which is the date on which the IOR commits to purchasing the asset.

On initial recognition, financial assets held for trading are recognized at fair value, which generally corresponds to the initial cash consideration paid, excluding direct transaction costs or revenues directly attributable to the instrument, which are recognized in the Income Statement.

Subsequent to initial recognition, the financial assets are measured at fair value, with any gains or losses arising from the change in fair value recognized in the Income Statement.

For the fair value measurement please refer to Section 1.4, Fair value information.

Disposals are recognized on the trade date which is the date on which the Institute commits to dispose the assets.

Gains and losses arising from disposal or redemption and unrealised gains and losses arising from changes in the fair value are recognized in the Income Statement, item 80 "Net trading result".

Interest income and expense arising from the financial assets held for trading are recognized in the Income Statement on an accrual basis and recognized "pro rata" based on the contractual interest rate. These are recognized in the Income Statement, item 10 "Interest and similar income".

Dividends on financial assets held for trading are recognized in the Income Statement, item 70 "Dividend income" when the entity's right to receive payment is established.

All financial assets held for trading are derecognized when the rights to receive cash flows from the financial assets have expired or when the IOR has substantially transferred all risks and rewards of ownership.

1.2.2 Financial assets available for sale

Financial Assets classified as Available for sale are those intended to be held for an indefinite period of time, and those that are subject to agreements that restrict the sale for a specified period.

In addition, financial assets classified available for sale include non-derivative financial assets that are not classified as held for trading or loans and receivables or held to maturity investments.

Financial assets available for sale are recognized on the trade date, which is the date on which the IOR commits to purchasing the asset.

Financial assets available for sale are initially recognized at fair value plus any direct transaction costs directly attributable to the instrument.

Financial assets available for sale are subsequently measured at fair value, and any changes in the fair value are recognized in Other Comprehensive Income and therefore directly in an equity reserve.

For the fair value measurement please refer to Section 1.4 "Fair value information".

Disposals are recognized on the trade date which is the date on which the Institute commits to dispose the assets.

At the time that the financial assets are derecognized or impaired, accumulated gain or loss from changes in the fair value of financial assets available for sale previously recognized in Other Comprehensive Income are reclassified and recognized in the Income Statement.

When the financial assets available for sale are sold, any unrealised gains or losses previously recognized in Other Comprehensive Income, are reclassified into the Income Statement, item 100 "Profit (loss) on disposal or repurchase" line b "Financial assets available for sale".

In case of impairment losses, gains or losses previously recognized in Other Comprehensive Income are transferred to the Income Statement item 130 "Net losses/reversal on impairment" line b "Financial assets available for sale".

At each balance sheet date, the IOR assesses whether there is objective evidence of impairment on financial asset available for sale. A significant or prolonged decline in the fair value of the financial asset below its cost is considered as objective evidence of a reduction in value. If there is such evidence, the cumulative loss, measured as the difference between the acquisition cost and the current fair value, less previously recognized impairment loss, is transferred from equity and recognized in the Income Statement in item 130 "Net losses/reversal on impairment" line b. If, in a subsequent period, the amount of the impairment loss decreases, impairment losses recognized in the Income Statement on equity instruments are not reversed through the Income Statement, but through the Fair Value Reserves, a component of equity. For debt instruments classified as available for sale, if the fair value increases in a subsequent period and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed through the Income Statement.

The impairment policy adopted by IOR is that all equity securities classified as available for sale must be impaired when their market prices are below their carrying prices and the price decline is more than 20%, or when the decline to below the acquisition cost has persisted for more than 36 months.

Interest income and expense arising from the financial assets available for sale are recognized in the Income Statement on an accrual basis and recognized "pro rata" based on the effective interest rate method. These are recognized in the Income Statement, item 10 "Interest and similar income".

Dividends on financial assets available for sale are recognized in the Income Statement, item 70 "Dividend income" when the entity's right to receive payment is established.

All financial assets available for sale are derecognized when the rights to receive cash flows from the financial assets have expired or when the IOR has substantially transferred all risks and rewards of ownership.

1.2.3 Financial assets held to maturity

Financial assets held to maturity are quoted non-derivative financial assets with fixed or determinable payments and with fixed maturities which the IOR has the intention and ability to hold to maturity. If the IOR sells financial assets held to maturity, the entire category must be reclassified as available for sale and for two subsequent years, no financial asset can be classified in this category.

Financial assets held to maturity are recognized at the trade date, which is the date on which the IOR commits to purchasing the asset, and are recognized at fair value plus any direct transaction costs.

The financial assets held to maturity are subsequently measured at amortised cost using the effective interest rate method, and adjusted to take into account the effects of any impairment losses, when applicable the circumstances described below.

Gains and losses on financial assets held to maturity are recognized in the Income Statement through the financial amortisation process (item 10 "Interest and similar income") or when the assets are derecognized (item 100 "Profit (loss) on disposal or repurchase" line c "Financial assets held to maturity") or when impairment losses are recognized in the Income Statement (item 130 "Net losses/reversal on impairment" line c "Financial assets held to maturity").

As of each balance sheet date, the IOR assesses whether there is objective evidence of impairment on financial asset held to maturity. A financial asset is impaired and impairment losses are recognized when one or more loss events occurred after the initial recognition of the asset and that loss event has an impact on the estimated future cash flows of the financial asset. The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is directly reduced and the extent of the loss is recognized in the Income Statement item 130 "Net losses/reversal on impairment" line c "Financial assets held to maturity".

Interest income and expense arising from the financial assets held to maturity are recognized in the Income Statement on an accrual basis and recognized "pro rata" based on the effective interest rate method. These are recognized in the Income Statement, item 10 "Interest and similar income".

The effective interest method is a method calculating amortized cost of an asset or a financial liability and of allocating interest. The effective interest rate is the rate that makes the present value of expected cash flows until maturity of the financial instrument (or, if more reliable for a shorter period) exactly equal to the current book value. The calculation not only includes all fees and premiums or discounts received or paid to the counterparty, which are an integral part of the effective interest rate, but also the transaction costs and all other premiums or discounts.

All financial assets held to maturity are derecognised when the rights to receive cash flows from the financial assets have expired or when the IOR has substantially transferred all risks and rewards of ownership.

1.2.4 Credits

This item includes loans to customers and banks, with fixed or determinable payments, provided directly, not quoted in an active market and not initially classified as financial assets held for trading, available for sale or at fair value.

This item includes:

1. deposits on demand and time deposits with banks;
2. authorized financing agreements where the Institute provides money directly to the customers without the intention of subsequent re-negotiation;
3. Loans and Receivables debt securities offered through private placements, which the Institute does not designate as financial assets at fair value through profit or loss or available for sale.

These financial assets are subject to the risk of deterioration of the creditworthiness of the counterparty.

Deposits with banks and financing agreements are recognized when the amount is advanced to the borrower. They are initially recognized at fair value, which is the value of the loan, plus any direct transaction costs. Financing agreements are subsequently measured at amortised cost using the effective interest rate method.

Securities are initially recognized on the trade date, which is the date on which IOR commits to purchasing the asset at fair value plus any direct transaction costs or income. Securities are subsequently measured at amortised cost using the effective interest rate method, and are subject to impaired test and impairment losses are recognized when one or more loss events occurred after the initial recognition of the asset and that loss event has an impact on the estimated future cash flows of the financial asset.

The amortized cost method is not used for short-term loans for which the effect of the application of the discounting logic is negligible. A similar valuation criterion is adopted for loans without a defined or revocation term.

Interest income and expense arising from loans and advances to customers are recognized in the Income Statement on an accrual basis and recognized "pro rata" using the effective interest rate method. These are recognized in the Income Statement, item 10 "Interest and similar income".

At each balance sheet date, the IOR assesses whether there is objective evidence of impairment. A financial asset is impaired and impairment losses are recognized when one or more loss events occurred after the initial recognition of the asset and that loss event has an impact on the estimated future cash flows of the financial asset.

The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced directly for securities or bank deposits, while for financing agreements through the use of a provision account. The extent of the loss is recognized in the Income Statement item 130 "Net losses/reversal on impairment" line a "Receivables".

Loans which are not individually impaired are subject to valuation on a portfolio basis based on historical data. The loss is recognized in the Income Statement item 130 "Net losses/reversal on impairment" line a "Receivables".

If, in a subsequent period, the impairment loss decreases and the decrease can be objectively attributed to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account for the financing agreements or by adjusting the carrying amount of the asset for securities and bank deposits. The amount of the reversal is recognized in the Income Statement, Statement item 130 "Net losses/reversal on impairment" line a "Receivables". In any case, the reversal can not exceed the cost that the financial instrument prior to the recognition of any impairment loss.

Credits are derecognized when the rights to receive cash flows from the financial assets have expired or when the IOR has substantially transferred all risks and rewards of ownership.

When a loan becomes uncollectible, it is written off against the related provision for loan impairment. Such exposures are written off after all the necessary procedures have been performed and the extent of the loss has been determined. Subsequent recoveries of amounts previously written off are recognized in the Income Statement item 130 "Net losses/reversal on impairment" line a "Receivables".

Regarding loans to customers, at the end of each month, the Advances Department analyses all exposures and submits to the Directorate a proposal on how to manage aged loans at risk for non-collection. Particularly, when the balance is deemed to be collectible within a short period, an impairment loss is not realized, but the trend is monitored; when the balance is deemed to be collectible in a mid/long term period, an impairment loss is recognized; when the positions are past due and uncollectible, the department proposes a write-off the amount as a loss on loans to the Directorate.

It is to be mentioned that the Institute is not authorized by the Autorità di Informazione Finanziaria to carry out the activity of "lending" (cfr. art. l (l) (b) of the Law n.XVIII and art. 3 (24) (b) of the Regulation No. l), as credit activities on its own. However, it is authorized to make "advances" that is to disburse funds to its clients and to a limited extent following guarantee of future income (such as, for example, in the case of the advance of salary or pension paid by the Holy See or the Governatorato of Vatican City) or guaranteed by financial assets of the same amount deposited by the clients at the Institute.

1.2.5 Derivative financial instruments and hedge accounting

Derivatives are initially recognized at fair value on the date in which a derivative contract is entered into.

The initial fair value generally corresponds to the initial cash consideration, and subsequently remeasured at fair value with changes recognized through profit or loss.

The fair value of derivatives quoted in active markets is based on current bid prices. If the market for a financial derivative is not active, the IOR obtains fair value from third parties or establishes fair value by using valuation models that are primarily based on objective financial inputs, as well as considering prices utilised in recent transactions and prices of similar financial instruments. All derivatives are recognized as assets when the fair value is positive and as liabilities when fair value is negative.

Derivative financial instruments may include embedded derivatives in a hybrid financial instrument.

IAS 39 requires that an embedded derivative be separated from its host contract and accounted for as a derivative when:

1. The economic risks and characteristics of the embedded derivative are not closely related to those of the host contract;
2. A separate instrument with the same terms as the embedded derivative would meet the definition of a derivative;
3. The hybrid (combined) instrument is not measured at fair value with changes in fair value recognized through Income Statement.

The Institute does not enter into Fair value hedges, Cash flow hedges or Net investment hedges for foreign currency transactions/positions.

As of 31 December 2017 and 2016, the Institute did not hold derivatives.

1.2.6 Investment in subsidiaries

Investment in subsidiaries consists of the stake in the wholly-owned real estate company S.G.I.R. S.r.l., based in Rome, Via della Conciliazione. The principal assets of this company are real estate properties.

Investment in subsidiaries is carried at cost, less impairment.

Real estate owned by the subsidiary is depreciated on a straight-line basis over its estimated useful life which management considers as between 30 and 50 years. Land is not depreciated.

1.2.7 Tangible assets

1.2.7.1 Tangible assets for investment - Investment properties

Investment properties are properties directly owned by the IOR. These are buildings not owner-occupied. They were inherited and held to generate rental income, capital appreciation or both.

Investment properties are initially measured at cost (which is zero in case of inheritances) and subsequently at fair value with any change recognized in the Income Statement, item 220 "Net result of fair value valuation of tangible and intangible assets".

Improvements to buildings increase their carrying amounts.

1.2.7.2 Tangible assets for business activities – Equipment, furniture and vehicles

All equipment, furniture and vehicles are stated at historical cost, minus accumulated depreciation. Historical cost is generally based on the fair value of the sum paid in exchange for assets and includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or are recognized as a separate asset, as appropriate, only when it is probable that the IOR will recognise future economic benefits associated with the item.

All repairs and maintenance costs are charged to the Income Statement in the year they are incurred.

Equipment, furniture and vehicles are amortised on a straight-line basis over their expected useful lives, usually measured in four years.

The asset's residual values and useful lives are reviewed, and adjusted if appropriate, on each balance sheet date. These assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

The result of the impairment test and the depreciations are recognized in the Income Statement item 170 "Net value adjustments to/recoveries on tangible assets".

Gains and losses on disposals are determined as the difference between the sale proceeds and the carrying amount of the assets. They are recognized in the Income Statement, under item 190 "Other operating income (expense)".

1.2.8 Intangible assets

Intangible assets correspond to computer software licenses and to expenses related to their implementation. Acquired computer software licenses are recognized at acquisition costs, including costs incurred to bring the specific software into use. These costs are amortised on a straight-line basis over their expected useful lives, usually measured in four years.

These assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell it and its value in use.

The results of the impairment test and depreciation are recognized in the Income Statement item 180 "Net value adjustments to/recoveries on intangible assets".

Costs associated with maintenance of computer software programmes are recognized as an expense in the Income Statement when they are incurred.

1.2.9 Due to banks and to customers

Due to banks comprises interim current accounts overdrafts, as the Institute does not carry out funding activites on the interbank market.

Due to customers are composed of financial instruments (different from trading liabilities) that assumed the typical forms of funds, realised by IOR with customers.

The mentioned financial liabilities are recorded in the financial statements at the trade date, which is the date when IOR receives the amounts. They are initially recognized at the current value, which normally corresponds to the amount collected. The initial recognition value includes possible expenses and incomes from anticipated transaction and directly attributable to each liability; not included in the initial carrying amount are all charges which are paid back by the credit counterparty or that are attributable to internal administrative expenses.

After the initial recognition, due to banks and to customers are measured at amortized cost using the effective interest rate method. The short-term liabilities remain recorded at the amount received.

Interest expense related to due to banks and to customers are recognized in the income statement, item 20 "Interest and similar expense".

Due to banks and to customers are derecognized when they expired or extinguished.

1.2.10 Legates

According to the Canon Law (Can. 1303), the term "Legati – non autonomous pious foundation" comprises: "temporal goods given in any way to a public juridical person and carrying with them a long-term obligation, such a period to be determined by particular law. The obligation is for the juridical person, from the annual income, to celebrate Masses, or to perform other determined ecclesiastical functions, or in some other way to fulfil the purposes mentioned in Can. 114, par. 2".

Based on such definition, this is understood to be an arrangement whereby capital is donated or willed to the IOR for religious or charitable purposes, based on the understanding that the transferred capital is invested on a long term basis and the annual income earned from the investment is devoted to the fulfilment of the purpose prescribed by the donor. Under these provisions, the IOR will administer the capital in accordance with the purpose prescribed by the donor (e.g., for Holy Mass Intention or scholarships).

Legates are recognised in the financial statement at the trade date. Legates are initially recognised at the current value, which normally corresponds to the amount received. The initial recognition value includes also expenses and incomes for anticipated transaction and directly attributable to each liability; not included in the initial carrying value are all charges which are paid back by the credit counterparty or that are attributable to internal administrative expenses.

After the initial recognition, Legates are measured at amortized cost using the effective interest rate method.

The interest expense related to the Legates are recognized in the income statement, item 20 "Interest and similar expense".

Legates are derecognised when they expired or extinguished.

1.2.11 Staff severance fund

Staff severance fund is a post-employment benefit that corresponds to indemnities paid to personnel when they leave the IOR. The amount due is based on years of service and salary paid in the last year of employment. These benefits are financed by contributions from employees and the IOR.

The liability is measured with utilizing certain actuarial assumptions, as the present value of the estimated future cash outflows according to the projected unit credit method required by IAS 19. Remeasurements arising from the defined benefit plan comprise actuarial gains and losses, recognized in Other Comprehensive Income. All other expenses related to the defined benefit plan in the Income Statement, item 150 "Administrative Expenses", line a "Staff expenses".

1.2.12 Provisions for risks and charges – Pension fund and similar obligations

For the pensions of its employees, the IOR operates a defined benefit plan, which is financed by contributions from employees and the IOR.

The IOR's net liabilities related to the defined benefit plan for pensions is calculated by estimating the amount of future benefit that employees will earn in return for their service in the current and prior periods; that benefit is discounted to determine its present value.

The IOR determines the interest expense on the defined benefit liability for the year by applying the discount rate used to measure the same liability at the beginning of the year.

The discount rate is the yield on the reporting date from high quality corporate bonds that have maturity dates approximating the terms of the IOR's liabilities and that are denominated in the currency in which the benefits are expected to be paid.

The calculation is performed annually by a qualified actuary, who assesses the fairness of the liability, using the projected unit credit method. Remeasurements arising from the defined benefit plan comprise actuarial gains and losses. The IOR recognizes them immediately in Other Comprehensive Income and all other expenses related to the defined benefit plan in the Income Statement, item 150 "Administrative expenses", line a "Staff expenses".

When the benefits of the plan are changed, the portion of the changed benefit related to past service by employees is recognized immediately in the Income Statement.

On 1 January 2005, all IOR personnel also joined the general Vatican City State pension plan. This system is financed by contributions made by the Institute and employees. Contributions to the Vatican plan made by the IOR are recognized in the Income Statement, item 150 "Administrative expenses", line a "Staff expenses" when they occur.

Consequently, the IOR's defined benefit plan for pensions covers the entire amount to be paid by the Institute to employees for their service up to 31 December 2004. For the employees' services from 1 January 2005, the obligation is limited to the part not covered by the Vatican City State Pension Plan taking into account the difference in the retirement age of the two pension systems.

1.2.13 Foreign Currency Transactions

Functional and presentation currency

The functional currency is the currency in which the items included in the financial statements must be measured. According to IAS 21 "The effects of changes in foreign exchange rates" the functional currency is the currency of the primary economic environment in which the entity operates. This is the currency that determines the pricing of transactions, but it is not necessarily the currency in which transactions are denominated.

The reporting currency is the currency in which the financial statements are prepared. IAS 21 allows an entity to prepare its financial statements in any currency.

The IOR's functional and presentational currency is the Euro, which is the currency of the primary economic environment in which the Institute operates.

Transactions and balances

Foreign currency transactions, if they impact profit or loss accounts, are converted into the functional currency using the exchange rates applicable at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are converted into the functional currency using the spot exchange rate at the reporting date (closing rate).

Non-monetary assets and liabilities denominated in foreign currencies are translated using the rate at the date their amount (cost or fair value) was determined: non-monetary items carried at cost are converted at the exchange rate at the date of initial recognition in the financial statements, while non-monetary items carried at fair value are translated using the rate at the date of the determination of their fair value.

Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the conversion at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the Income Statement, item 80 "Net income for trading activities".

Foreign exchange gains and losses resulting from the conversion at year-end exchange rates of non-monetary assets and liabilities are:

- recognized in the Income Statement as part of the fair value gain or loss if the non-monetary assets and liabilities are carried at fair value through profit and loss;
- included in the fair value reserves in the equity if the non-monetary assets and liabilities are carried at fair value in the equity.

1.2.14 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount is reported on the Balance Sheet only when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis. Otherwise, the financial assets and liabilities are separately reported on the balance sheet.

1.3 Transfers between Portfolios

The amendments to IAS 39 and to IFRS 7 allow for the reclassification of certain financial assets after their initial recognition, out of the held for trading (HFT) and available for sale (AFS) portfolios.

In particular, those HFT or AFS financial assets that would have met the definition specified by international accounting standards for the loan portfolio (if such assets were not classified as HFT or AFS respectively on initial recognition) may be reclassified if the entity intends, and is able, to hold them for the foreseeable future or until maturity.

The Institute did not have any transfers between portfolios in 2017 and in previous years.

1.4 Fair Value Information

Qualitative fair value information

For the measurement of fair value, the amendments to IFRS 7 and subsequent changes introduced by IFRS 13 defines a fair value hierarchy based on level of observable inputs used for measurement. The financial assets are classified according to the following hierarchy that consists of three levels.

Level 1

In Level 1, the fair value is measured using the quoted prices in active markets for the financial assets and liabilities to be evaluated.

A financial instrument is considered quoted in an active market when its price is:

- readily and regularly available on stock exchanges, from information providers or intermediaries;
- significant, meaning that it represents effective market

transactions regularly occurring in normal transactions.

To be considered Level 1, the price should not be adjusted through an adjustment factors (valuation adjustment). If it is adjusted, the measurement at fair value of financial instrument will be Level 2 or Level 3.

Level 2

A financial instrument is included in Level 2 when the inputs utilised to measure fair value are directly or indirectly observable in the market.

The parameters of Level 2 are as follows:

- prices quoted on active markets for similar assets or liabilities;
- price quoted on non-active markets for similar or identical assets and liabilities;
- market observable inputs other than the quoted price for the asset or liability (interest rates, yield curve, credit spreads, volatility);
- parameters that derive mainly (or are corroborated by correlation or other techniques) from observable market data (market-corroborated inputs).

An input is observable when it reflects the assumptions that market participants would use in pricing an asset or liability based on market data provided by sources independent of the reporting entity.

Valuation techniques used to determine fair value that should be used when the market price is not available or is not significant, must meet three conditions. They must:

1. be methodologically consolidated and widely accepted;
2. utilise market inputs disclosed above;
3. be periodically reviewed.

Valuation techniques used for fair value measurement should be periodically assessed using inputs observable in the markets to ensure that outputs reflect actual data and comparative market prices and to identify any weaknesses.

If the fair value measurement utilise observable inputs that require a significant adjustment based on unobservable inputs, the financial instrument should be considered in Level 3.

Level 3

Included in Level 3 are financial instruments valued using unobservable market data (unobservable inputs). To be included in Level 3, at least one of the inputs must be unobservable on the market.

Level 3 financial instruments are valued using inputs that are not derived from independent sources, rather they are based on the reporting entity's own assumptions based on assumptions that market participants would use, based on observable inputs.

IFRS 13 specifies a hierarchy of fair value measurements based on whether the inputs are observable or unobservable. Observable inputs reflect the assumptions that market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. The market price is the most observable and objective input (Level 1). Where no active markets exists or where quoted prices are not available, the entity determines the fair values by using valuation techniques. Valuation techniques can utilise inputs observable on the market (Level 2) or non-observable inputs (Level 3).

The above mentioned valuation approaches should be applied in a hierarchical order.

When there is availability of quoted market prices in active markets, an entity must measure fair value using Level 1 inputs. Furthermore, the valuation techniques used should prioritise the utilization of inputs observable on the market and should rely as little as possible on the reporting entity's own data, internal valuations or unobservable inputs.

Fair value Level 2 and 3: valuation techniques and input used

The criteria used by the IOR to determine the fair value of financial instruments are as follows.

The fair values of investments held by the IOR quoted in active markets are usually based on current bid prices.

A financial instrument is considered as quoted in active markets if the prices are readily and regularly available in an exchange or regulatory agency and those prices represent actual market transactions that occur regularly on an arm's length basis.

In the absence of an active market, or in the event the market at the time of the valuation is not considered active, for example, in case of illiquid markets, the valuation techniques adopted by IOR are based on the use of recent arm's length transactions in the market, even on a non-active market, relative to identical financial instrument or financial instruments with similar characteristics. The valuation techniques include the discounted cash flow analysis and other valuation techniques commonly used by market participants.

If recent transactions of the same or similar instruments are not available, the IOR uses valuation techniques based on market parameters or other parameters.

When using valuation techniques, the IOR tries to use observable market data, reducing its reliance on internal data.

Valuation techniques are periodically reviewed for applicability, assessing the quantity and the quality of information available as of the balance sheet date, in order to correctly reflect any changes in the market. For the same reason, adjustments to market inputs, utilised in a certain model, can change from time to time.

Consequently IOR models ensure that outputs reflect actual data and comparative market prices.

In Level 1, the IOR has classified all financial instruments quoted in active markets.

Under Level 2, the IOR has classified all illiquid financial instruments, include those that are structured or unstructured, as well as listed external investment funds that are not immediately payable and unlisted investment funds with investments in listed instruments. The basis for the valuation of illiquid securities follow prices provided by the securities issuer. These prices are internally verified and tested utilising internal models and observable market parameters and, in case of discrepancies, adjusted considering the result of the above-mentioned analysis. They are also adjusted on the basis of valuations from independent sources.

Under Level 3, the IOR has classified equity securities that are not quoted or other financial instruments for which fair values are determined using a model based on internal parameters.

To the extent that this is practical, the models use only observable data. However, areas such as default rates, volatilities and correlations require the Directorate to make estimates.

In this category the Institute has also classified other assets:

- for which the IOR did not receive independent valuations;
- for which the IOR does not have access to financial information;
- for which, despite having financial information, the Institute believes that the valuation of underlying assets, due to the nature of the investment, is based on valuation parameters that are not immediately observable in the market;
- for which the IOR has received independent expert valuations (i.e. for investment properties).

The NAV of investment funds, defined as the difference between the current value of the assets and liabilities of the fund, a Fair Value Adjustment was calculated to include other risk factors.

The Fair Value Adjustment (FVA) is defined as the amount to be added to the mid-price observed in markets, rather than the price determined by the model, with the aim of obtaining the fair value of the position. The FVA includes the uncertainty inherent in the valuation of a financial instrument with the goal of reducing the risk of incorrect valuations in the financial statements and ensuring that fair value reflects the realised price of a market transaction that is actually possible; and incorporating possible future costs.

The Institute adjusts the value of financial instruments measured at fair value on a recurring basis classified as Level 2 and Level 3 based on credit risk (Credit Valuation Adjustment), liquidity risk related to the disinvestment, close-out costs and available informations about the outstanding assets.

With regard to the Credit Valuation Adjustment, the Institute considered the impact of fair value on credit risk of the counterparty and the country using the following inputs:

- PD (Probability of Default) linked to the rating of counterparty (if not available the PD corresponding to an investment with an S&P rating of BBB was used);
- LGD (Loss Given Default) based on the estimated level of expected recovery in case of counterparty default and defined through market benchmark and based on experience. The percentage used was 60%.

Regarding the close-out cost, an adjustment is applied on the NAV of external investment funds if close-out penalties are stipulated.

Sensitivity Analysis

For fair value measurements where significant unobservable inputs are used (Level 3), a sensitivity analysis is performed in order to obtain the range of reasonable alternative valuations. The Institute takes into account that the impact of unobservable inputs on the measurement of fair value of Level 3 depends on the correlation between the different inputs used in the valuation process.

A sensitivity analysis was performed using a stress test on the PD and LGD by +/-5% and it did not have a significant impact to the value of the investments classified as Level 3.

Fair value hierarchy (transfers between portfolios)

With reference to financial assets and liabilities measured at fair value on a recurring basis, transfers between the fair value hierarchy were based on the following guidelines.

For debt securities, transfers from Level 3 to Level 2 occur when the relevant parameters used as inputs to the valuation technique are observable on the market. Transfers from Level 3 to Level 1 occur when the presence of an active market has been verified, as defined by IFRS 13. Transfers from Level 2 to Level 3 occur when some of the relevant parameters for determination of fair value are no longer directly observable on the market.

For equity instruments classified as available- for- sale, transfers between the fair value hierarchy occur:

- during the period, when market observable inputs become available (e.g. prices are determined in comparable transactions on the same instrument between independent and knowledgeable counterparties), the Institute proceeds with the reclassification from Level 3 to Level 2;

- when inputs that are directly or indirectly observable in the market used as the basis for the valuation no longer exist, or no longer updated (e.g. No recent comparable transactions or market multiples are no longer applicable) and no other inputs are available, the Institute uses valuation techniques that use unobservable inputs, proceeding with the reclassification from Level 2 to Level 3.

Information on assets measured at fair value on a recurring basis

We provide below the IFRS 13 disclosure requirements about assets measured at fair value on a recurring basis. By definition, the carrying value of these items corresponds to the fair value.

Fair value is defined as the price that would be received in selling an asset or paid when transferring a liability in an ordinary transaction between market participants at the measurement date (i.e. an exit price).

Financial assets held for trading

These consist of:

- **Debt securities**: the Institute has investments in debt securities valued at market price (mark-to-market) and regularly traded in active, liquid markets. Consequently, these instruments are classified as Level 1 in the fair value hierarchy, except for some bonds whose prices are determined internally on the basis of similar instruments quoted on active markets and are classified as Level 2; these amounted to EUR 26.9m.
- **Equity securities**: the Institute has investments in equity securities valued at market price (mark-to-market) and regularly traded in active, liquid markets. Consequently, these instruments classified as Level 1 in the fair value hierarchy.
- **Investments funds**: the Institute has external investment funds amounting to EUR 32.6m. With the exception of a fund of EUR 10.3m as Level 2 (liquid with monthly NAV), investment funds are classified as Level 3. Consequently, at 31 December 2017, a total of EUR 10.3m was classified as Level 2, while the remaining amount for EUR 22.3m was Level 3.

Financial assets available for sale

These are mainly classified as Level 1, comprise of shares quoted in active, liquid markets, except for two unlisted equity securities, one classified as Level 2 and the other classified as Level 3.

Tangible assets for investment

This item is comprised of properties directly owned by the Institute.

The fair value of the properties is assessed by a qualified, independent expert.

The appraisal is based on the real estate market data collected through surveys carried out by major industry players. The parameters used also reflect expert assumptions based on available information. For these reasons, the investment properties are classified as Level 3 on the fair value hierarchy.

Assets not measured at fair value on a recurring basis

For assets and liabilities not measured at fair value on a recurring basis, the following information is required by IFRS 13.

Financial assets held to maturity

The fair value of financial assets held to maturity corresponds to the market value at the balance sheet date. The securities are classified as Level 1 in the fair value hierarchy since they are regularly traded on active, liquid markets.

Due from banks

This item is comprised of deposits on demand and time deposits with banks in addition to financial "Loans and Receivables" securities issued by banks.

Assuming that time deposits do not exceed ninety days, the carrying value of bank deposits, at the balance sheet date, approximates fair value and they are recorded in Level 1 of the fair value hierarchy.

For "Loans and Receivables" securities, the fair value represents the market value at the closing date of the financial statements.

By definition, "Loans and Receivables" securities are not quoted in active, liquid markets, but the valuation is sent weekly by the counterparty and is verified through an internal model.

For these reasons, "Loans and Receivables" securities are classified in Level 2 of the fair value hierarchy.

Due from customers

This item is comprised of receivables due from credits granted as advances to clients in addition to "Loans and receivables" securities issued from entities other than banks.

For Doubtful loans considered to be non-collectible, the Institute proceeded in the calculation of a specific impairment loss, and the carrying value represents fair value.

With regards to other receivables, the fair value was calculated as follows:

- Loans and credit lines: calculated by discounting future cash flows using a discount rate representative rate for the Institute;

- temporary Overdrafts: given their nature, the value of overdrafts approximates fair value.

For "Loans and Receivables" securities the fair value represents the market value at the closing date of the financial statements.

By definition, "Loans and Receivables" securities are not quoted in active, liquid markets, but the valuation is sent weekly by the counterparty and is controlled through an internal model.

For these reasons, "Loans and Receivables" securities are classified in Level 2 of the fair value hierarchy.

Liabilities not measured at fair value on a recurring basis

Due to banks

The carrying value of this item approximates fair value, considering their short maturity.

Due to customers

This item is comprised of client deposits on demand and time deposits, liquid accounts and term deposits related to Asset Management positions. Their carrying value approximates fair value, considering the short maturity or indefinite maturity.

As the fair value calculation is based on parameters not observable on markets, not even indirectly, these are classified as Level 3 in the fair value hierarchy.

1.4.2 Quantitative fair value information

1.4.2.1 Fair value hierarchy

(a) Assets and liabilities measured at fair value on a recurring basis: detail by fair value level

Assets and liabilities measured at fair value	2017			2016		
	L1	L2	L3	L1	L2	L3
1. Financial assets held for trading	2,057,336	37,181	22,254	1,802,904	91,923	23,277
2. Financial assets carried at fair value						
3. Financial assets available for sale	3,879	684	8	6,157	499	8
4. Hedging derivatives						
5. Tangible assets			3,102			2,980
6. Intangible assets						
Total	**2,061,215**	**37,864**	**25,364**	**1,809,061**	**92,422**	**26,265**
1. Financial liabilities held for trading						
2. Financial liabilities carried at fair value						
3. Hedging derivatives						
Total						

Key: L1 = Level 1 L2 = Level 2 L3 = Level 3

(b) Annual changes of assets measured at fair value on a recurring basis (Level 3)

The following table provides information about the assets measured at fair value on a recurring basis and categorized as Level 3 in the fair value hierarchy at the beginning of the year, disposals and/or additions during the year, and their final values at the balance sheet date.

	Financial assets held for trading	Financial assets available for sale	Tangible assets
1. Opening balance	**23,277**	**8**	**2,980**
2. Additions			
2.1.Purchases			
2.2.Profit recognized in:			
2.2.1.Income Statement	392		136
- of which Gains	258		136
2.2.2 Net Equity			
2.3.Transfers from other levels			
2.4 Other variations in addition			
3. Disposals			
3.1 Sales			
3.2 Reimbursement	(400)		
3.3 Losses recognized in:			
3.3.1 Income Statement	(1,015)		(14)
- of which Losses	(1,015)		(14)
3.3.2 Net Equity			
3.4. Transfers to other levels			
3.5 Other variations in reduction			
4. Closing balance	**22,254**	**8**	**3,102**

((c) Annual changes of liabilities measured at fair value on a recurring basis (Level 3)

The Institute did not hold liabilities measured at fair value on a recurring basis.

d) Assets and liabilities not measured at fair value or measured at fair value on a non-recurring basis: detail by fair value level

	2017				2016			
	BV	**L1**	**L2**	**L3**	**BV**	**L1**	**L2**	**L3**
1. Financial assets held to maturity	246,168	259,547			558,956	583,392		
2. Due from banks	473,386	473,386			643,229	643,229		
3. Due from customers	25,423			26,242	29,153			30,418
Total	**744,977**	**732,933**		**26,242**	**1,231,338**	**1,226,621**		**30,418**
1. Due to banks	4,096	4,096						
2. Due to customers	2,131,421			2,131,421	2,398,924			2,398,924
Total	**2,135,517**	4,096		**2,131,421**	**2,398,924**			**2,398,924**

Key: BV = Book Value L1 = Level 1 L2 = Level 2 L3 = Level 3

1.5 Information on "day one profit/loss"

The Institute did not earn day one profit/loss from financial instruments pursuant to paragraph 28 of IFRS 7 and other related IAS/IFRS.

PART 2. INFORMATION ON THE BALANCE SHEET

ASSETS

ITEM 10 - CASH AND CASH EQUIVALENTS

Detail

	2017	2016
(a) Cash	15,247	15,216
(b) Free deposits ex art. 9 (b)	55,987	35,634
(c) Free deposits ex art. 9 (c)		
(d) Other free deposits		
Total	**71,234**	**50,850**

The balance included in (b) represent free deposits with Public Authorities of the Holy See and Vatican City State with the statutory purpose of administering the assets owned by the Holy See (at present APSA).

ITEM 20 ASSETS - FINANCIAL ASSETS HELD FOR TRADING

2.1 Detail by asset type

	2017			2016		
	L1	L2	L3	L1	L2	L3
A. Cash assets						
1. Debt securities						
1.1. Structured securities						
1.2. Other debt securities	2,027,677	26,855		1,750,174	81,519	
2. Equity securities	29,659			52,730		
3. UCI units		10,326	22,254		10,404	23,277
4. Loans						
4.1. Outstanding repos						
4.2. Other						
Total A	**2,057,336**	**37,181**	**22,254**	**1,802,904**	**91,923**	**23,277**
B. Derivatives						
1. Financial derivatives						
1.1. Held for trading						
1.2. Related to the *fair value option*						
1.3. Other						
2. Credit derivatives						
2.1. Held for trading						
2.2. Related to the *fair value option*						
2.3. Other						
Total B						
Total (A+B)	**2,057,336**	**37,181**	**22,254**	**1,802,904**	**91,923**	**23,277**

The table shows all financial assets, by type, allocated to the trading portfolio and classified in the fair value hierarchy (L1, L2 or L3) according to their nature.

UCI units in the financial assets held for trading refers exclusively to investment funds managed by third parties composed by equity securities. Regarding the composition of the funds, refer to the table included in section 5.2.6 "Information on unconsolidated structured entities" of Part 5 "Information on risks and hedging policies".

Financial assets held for trading is primarily comprised of debt securities classified as Level 1 in the fair value hierarchy; the only financial assets classified as Level 3 are shares of UCI units.

As of 31 December 2017, similar to the prior year, the Institute did not have any derivative financial instruments in the trading portfolio.

2.2 Detail by borrowers/issuers

	2017	2016
A. Cash assets		
1. Debt securities		
(a) Public entities	1,198,653	912,466
(b) Financial companies	675,554	703,239
(c) Insurance companies	5,115	9,286
(d) Non financial companies	175,211	206,702
(e) Other subjects		
2. Equity securities		
(a) Banks		
(b) Other issuers:		
- insurance companies	4,125	2,759
- financial companies	10,748	36,529
- non financial companies	14,786	13,442
- other		
3. UCI units	32,580	33,681
4. Loans		
(a) Public entities		
(b) Financial companies		
(c) Insurance companies		
(d) Non financial companies		
(e) Other subjects		
Total A	**2,116,771**	**1,918,104**
B. Derivatives		
(a) Banks		
(b) Customers		
Total B		
Total (A+B)	**2,116,771**	**1,918,104**

No borrowers/issuers are residents of the Vatican City State.

Line (a) "Public entities" of the item A.1 Debt securities is exclusively comprised of securities issued by Foreign Central Public Administrations.

In the portfolio of financial assets held for trading, there are no equity securities classified as in default or at the risk of default.

ITEM 40 ASSETS - FINANCIAL ASSETS AVAILABLE FOR SALE

4.1 Detail by asset type

	2017			2016		
	L1	L2	L3	L1	L2	L3
1. Debt securities						
1.1. Structured securities						
1.2. Other debt securities						
2. Equity securities						
2.1. Carried at fair value	3,879	684		6,157	499	
2.2. Carried at cost			8			8
3. UCI units						
4. Loans						
Total	**3,879**	**684**	**8**	**6,157**	**499**	**8**

4.2 Detail by borrowers/issuers

	2017	2016
A. Cash assets		
1. Debt securities		
(a) Public entities		
(b) Financial companies		
(c) Insurance companies		
(d) Non financial companies		
(e) Other subjects		
2. Equity securities		
(a) Banks		
(b) Other issuers:		
- insurance companies	3,880	6,157
- financial companies	684	499
- non financial companies	8	8
- other		
3. UCI units		
4. Loans		
(a) Public entities		
(b) Financial companies		
(c) Insurance companies		
(d) Non financial companies		
(e) Other subjects		
Total A	**4,572**	**6,664**

No borrowers/issuers are resident in the Vatican City State.

In the portfolio of financial assets available for sale, there are no equity securities classified in default or at the risk of default.

4.3 Financial assets available for sale with specific hedges

The Institute did not hold financial assets available for sale with specific hedges.

ITEM 50 ASSETS - FINANCIAL ASSETS HELD TO MATURITY

5.1 Detail by asset type

	2017				2016			
	VB	FV			VB	FV		
		L1	L2	L3		L1	L2	L3
1. Debt securities								
- structured								
- other	246,168	259,547			558,956	583,392		
2. Loans								
Total	**246,168**	**259,547**			**558,956**	**583,392**		

Key: BV = book value, FV = fair value

Financial assets held to maturity is mainly comprised of government bonds issued by European countries and bonds issued by international financial entities.

As of 31 December 2017, securities with maturity less than 1 year (31 December 2018) had a balance sheet value amounting to EUR 94.7m.

5.2 Detail by borrowers/issuers

	2017	2016
1. Debt securities		
(a) Public entities	160,670	441,580
(b) Financial companies	67,338	88,033
(c) Insurance companies		
(d) Non financial companies	18,160	29,343
(e) Other subjects		
2. Loans		
(a) Public entities		
(b) Financial companies		
(c) Insurance companies		
(d) Non financial companies		
(e) Other subjects		
Total	**246,168**	**558,956**

No borrowers/issuers are residents of the Vatican City State.

Line (a) Public entities of the item A.1 Debt securities is exclusively comprised of securities issued by Foreign Central Public Administrations.

5.3 Financial assets held to maturity with specific hedges

The Institute did not hold financial assets held to maturity with specific hedges.

ITEM 60 ASSETS – DUE FROM BANKS

6.1 Detail by type

	2017				2016			
	VB	FV			VB	FV		
		L1	L2	L3		L1	L2	L3
A. Credits ex art. 14 (c)								
1. Fixed-term deposits	57,058	57,058			77,104	77,104		
2. Outstanding repos								
3. Others								
B. Credits ex art. 14 (d)								
1. Fixed-term deposits								
2. Outstanding repos								
3. Others								
C. Due from banks								
1. Loans								
1.1. Current accounts and demand deposits	362,123	362,123			457,624	457,624		
1.2. Outstanding repos	54,205	54,205			108,501	108,501		
1.3. Other loans:								
(a) Outstanding repos								
(b) Finance lease								
(c) Other								
2. Debt securities								
2.1. Structured securities								
2.2 Other debt securities								
Total	**473,386**	**473,386**			**643,229**	**643,229**		

Key: BV = book value, FV = fair value

No asset impairment was recorded.

Line A. Credits ex art. 14 (c) is comprised of different deposits from free deposits held with the Public Authorities of the Holy See and Vatican City State with the statutory purpose of administering the assets owned by the Holy See (at present, APSA).

6.2 Credits with specific hedges

The Institute did not hold credits with specific hedges and it has no outstanding finance leases.

ITEM 70 ASSETS – DUE FROM CUSTOMERS

7.1 Detail by type

	2017						2016					
	Book value			Fair value			Book value			Fair value		
	Non impaired	Impaired					Non impaired	Impaired				
		Purch-ased	Other	L1	L2	L3		Purch-ased	Other	L1	L2	L3
A. Loans												
1. Current accounts	11,253					11,253	8,424		27			8,451
2. Outstanding repos												
3. Mortgages												
4. Credit cards, personal loans and loans on salary												
5. Finance leases												
6. Factoring												
7. Other loans	7,200		6,969			14,989	12,495		8,207			21,967
B. Debt securities												
1. Structured securities												
2. Other debt securities												
Total	**18,453**		**6,969**			**26,242**	**20,919**		**8,234**			**30,418**

Additional supporting information is provided in Part 5 "Information on risks and related hedging policies" of this document.

It is to be mentioned that the Institute is not authorized by the Autorità di Informazione Finanziaria to carry out the activity of "lending" (cfr. art. l (l) (b) of the Law n.XVIII and art. 3 (24) (b) of the Regulation No. l), as credit activities on its own. However, it is authorized to make "advances" that is to disburse funds to its clients and to a limited extent following guarantee of future income (such as, for example, in the case of the advance of salary or pension paid by the Holy See or the Governatorato of Vatican City) or guaranteed by financial assets of the same amount deposited by the clients at the Institute.

7.2 Detail by borrowers

	2017			2016		
	Non impaired	Impaired		Non Impaired	Impaired	
		Purchased	Other		Purchased	Other
1. Debt securities						
(a) Public Entities						
(b) Financial companies						
(c) Insurance companies						
(d) Non financial companies						
(e) Other subjects						
2. Loans to:						
(a) Public Entities	11,238			8,290		
(b) Financial companies						
(c) Insurance companies						
(d) Non financial companies	2,908			3,315		
(e) Other subjects	4,307		6,969	9,314		8,234
Total	**18,453**		**6,969**	**20,919**		**8,234**

7.3 Credits with specific hedges

The Institute did not hold credits with specific hedges.

ITEM 100 ASSETS – INVESTMENT IN SUBSIDIARIES

10.1 Information on investment in subsidiaries

The Institute holds a financial investment in a real estate company, S.G.I.R. S.r.l., which is based in Italy and is 100% owned by the IOR.

10.2 Material investments in subsidiaries: book value, fair value and dividends received

The value of the investment in the real estate company S.G.I.R. S.r.l. was EUR 15.8 m.

There was no change in the value of the investment during 2017 and no dividends were paid.

The equity of S.G.I.R. S.r.l. as of 31 December 2017 was EUR 23.2m (2016: EUR 22.6m), including EUR 12.4m (2016: EUR 12.4m) for a Fiscal Revaluation Reserve.

As the investment is in an unlisted company, IOR has not carried out the measurement of the fair value.

In 2016, S.G.I.R. S.r.l. presented the “Social Report” to highlight the social benefits produced by the management of real estate assets that are not exclusively focused on profit. In fact, S.G.I.R. S.r.l. grants some properties for rent with subsidized rent or on loan for free use to support institutions with a social purpose, as notably discoled in the Chapter 2. Operational Information in the Management Report.

10.3 Material investment in subsidiaries: financial information

	Cash and cash equivalents	Financial assets	Non financial assets	Financial liabilities	Non financial liabilities	Total income	Interest margin	Value adjustments and write-backs on tangible and intangible assets	Profit (loss) from current operations before taxes	Profit (loss) from current operations after taxes	Profit (loss) from groups of assets being disposed after taxes	Profit (loss) for the year (1)	Other income items after taxes (2)	Compre-hensive income (3) = (1) + (2)
A. Subsidiaries entities														
S.G.I.R. S.r.l.	179	690	25,802	3,428	46	1,843		-19	1,032	630		630		**630**
B. Entities subject to joint control														
C. Entities subject to significant influence														

ITEM 110 ASSETS –TANGIBLE ASSETS

11.1 Tangible assets in-use: detail of the assets measured at cost

	2017	2016
1. Owned assets		
(a) land		
(b) buildings		
(c) furniture	1	1
(d) electronic equipment	144	115
(e) other		
2. Assets acquired under finance lease		
(a) land		
(b) buildings		
(c) furniture		
(d) electronic equipment		
(e) other		
Total	**145**	**116**

11.4 Tangible assets held for investment: detail of the assets measured at fair value

	2017				2016			
	VB	FV			VB	FV		
		L1	L2	L3		L1	L2	L3
1. Owned assets								
(a) land								
(b) buildings	3,102			3,102	2,980			2,980
2. Assets acquired under finance lease								
(a) land								
(b) buildings								
Total	**3,102**			**3,102**	**2,980**			**2,980**

Key: BV = book value, FV = fair value

11.5 Tangible assets in- use: annual changes

	Land	Buildings	Furniture	Electronic equipment	Other	Total
A. Opening balance			2,629	4,448	32	**7,109**
A.1 Net total adjustments			(2,628)	(4,333)	(32)	**(6,993)**
A.2 Net opening balance			1	115		**116**
B. Increases:						
B.1 Purchases				98		**98**
B.2 Capitalised improvement costs						
B.3 Write-backs						
B.4 Positive fair value differences recognized in						
a) Net Equity						
b) Income Statement						
B.5 Positive foreign exchange differences						
B.6 Transfer from investment property						
B.7 Other changes						
C. Decreases:						
C.1 Sales						
C.2 Depreciation				(69)		**(69)**
C.3 Impairment losses recognized in:						
a) Net Equity						
b) Income Statement						
C.4 Negative fair value differences recognized in						
a) Net Equity						
b) Income Statement						
C.5 Negative foreign exchange differences						
C.6 Transfer to:						
a) investment property						
b) assets being disposed						
C.7 Other changes						
D. Net closing balance			2,629	4,546	32	**7,207**
D.1 Total net adjustments			(2,628)	(4,402)	(32)	**(7,062)**
D.2 Gross closing balance			1	144		**145**

All tangible assets in-use were measured at cost.

11.6 Tangible assets held for investment: annual changes

	Total	
	Land	Buildings
A. Opening balance		2,980
B. Increases:		
B.1 Purchases		
B.2 Capitalised improvement costs		
B.3 Positive fair value differences		136
B.4 Write-backs		
B.5 Positive foreign exchange differences		
B.6 Transfer from tangible assets for functional use		
B.7 Other changes		
C. Decreases		
C.1 Sales		
C.2 Depreciation		
C.3 Negative fair value differences		(14)
C.4 Impairment losses		
C.5 Negative foreign exchange differences		
C.6 Transfer to other assets		
a) tangible assets for functional use		
b) current assets being disposed		
C.7 Other changes		
D. Closing balance		**3,102**

All the tangible assets held for investment are measured at fair value.

The item includes 5 investment properties received in the past through donations, totaling EUR 3.1m. The item increased from 31 December 2016 due to an increase in fair values.

The Institute has surveys performed by a qualified independent expert.

As of 31 December 2017, the properties did not generate any rental income, because the Institute signed a lease agreement with its subsidiary S.G.I.R. S.r.l. for the use of properties for free. During 2017, S.G.I.R. S.r.l. earns EUR 57,000 as rental income on these properties.

ITEM 120 ASSETS – INTANGIBLE ASSETS

12.1. Detail by asset

	2017		2016	
	Definite life	Indefinite life	Definite life	Indefinite life
A.1. Goodwill				
A.2. Other intangible assets				
A.2.1 Assets carried at cost:				
(a) intangible assets generated internally				
(b) other assets	871		1,044	
A.2.2 Assets carried at fair value				
(a) intangible assets generated internally				
(b) other assets				
Total	**871**		**1,044**	

Intangible assets consist of software programs and costs incurred to implement them.

12.2 Annual changes

	Goodwill	Other intangible assets generated internally		Other intangible assets: other		Total
		DEF	INDEF	DEF	INDEF	
A. Opening balance				7,081		**7,081**
A.1 Total net adjustments				(6,037)		**(6,037)**
A.2 Net opening balance				1,044		**1,044**
B. Increases						
B.1 Purchases				316		**316**
B.2 Increases of intangible assets generated internally						
B.3 Write-backs						
B.4 Positive fair value differences recognized in						
- Net Equity						
- Income Statement						
B.5 Positive foreign exchange differences						
B.6 Other changes						
C. Decreases						
C.1 Sales						
C.2 Impairment losses						
- Depreciation				(489)		**(489)**
- Write downs recognized in						
+ Net Equity						
+ Income Statement						
C.3 Negative fair value differences recognized in						
- Net Equity						
- Income Statement						
C.4 Transfer to non-current assets being disposed						
C.5 Negative foreign exchange differences						
C.6 Other changes						
D. Net closing balance				7,397		**7,397**
D.1 Total net adjustments				(6,526)		**(6,526)**
E. Gross closing balance				871		**871**

Intangible assets are carried at cost.
The IOR does not have internally generated intangible assets.

ITEM 150 ASSETS - OTHER ASSETS

15. Other Assets

	2017	2016
1.Gold	22,392	22,394
2. Medals and precious coins	10,536	10,490
3. Securities sold not settled	92	
4. Commission from asset management services not yet received	6,225	6,463
5. Client Tax advances	610	
6. Deposit for guarantees for credit cards transactions	702	799
7. Sundry debtors	451	833
8. Prepayments	494	980
Total	**41,502**	**41,959**

Gold is mainly deposited with the U.S. Federal Reserve, while medals and precious coins are kept in the IOR vaults.

Gold is carried at the lower of cost or net estimated recoverable amount.

Medals and precious coins are appraised on the basis of their weight and the quality of gold and silver they contain, carried at the lower of cost or net estimated recoverable amount.

Gains and losses arising from disposal of gold, medals and precious coins are recognized in the Income Statement, item 80 “Net trading result”. Losses arising from evaluation at the lower of cost or net estimated recoverable amount, as well as reversals of the previously recognized loss are recognized in the Income Statement, item 190 “Other operating income (expense)”.

Also included in Other Assets are commission from asset management services not yet received at the closing date of the financial statements for EUR 6.2m. These commissions, pertaining to the second half of 2017, were collected at the beginning of 2018.

LIABILITIES

ITEM 10 LIABILITIES - DUE TO BANKS

1.1 Detail by product

	2017	2016
1. Due to Public Authorities		
of which:		
- Public Authorities ex art. 24 (c)		
2. Due to foreign Public Authorities		
of which:		
- Public Authorities ex art. 24 (d)		
3. Due to banks		
3.1. Current accounts and demand deposits	4,096	
3.2. Fixed-term deposits		
3.3. Loans		
3.3.1. Reverse repos		
3.3.2. Other		
3.4. Amounts due under repurchase agreements of own equity instruments		
3.5. Other liabilities		
Total	**4,096**	
Fair value - level 1	4,096	
Fair value - level 2		
Fair value - level 3		
Total fair value	**4,096**	

Due to banks include amounts due to the Holy See and Vatican City State Public Authorities, the statutory purpose of which is to administer the Holy See's proprietary assets (at present APSA).

Amounts due as of 31 December 2017 was EUR 4.1m comprised payment orders to be paid in 2 days.

1.2 Subordinated liabilities

There are no subordinated liabilities recognized in this item.

ITEM 20 LIABILITIES – DUE TO CUSTOMERS

2.1 Detail by type

	2017	2016
1. Current accounts and demand deposits	2,121,947	2,397,688
2. Fixed-term deposits	9,474	1,236
3. Loans		
3.1. Reverse repos		
3.2. Other		
4. Amounts due under repurchase agreements of own equity instruments		
5. Other payables		
Total	**2,131,421**	**2,398,924**
Fair value - level 1		
Fair value - level 2		
Fair value - level 3	2,131,421	2,398,924
Total fair value	**2,131,421**	**2,398,924**

Due to customers had a decrease from 2016 due to the impact of Forex on US Dollars deposits as well as tax payments on financial instruments made through the Institute.

The above amounts include liquidity and term deposits related to the Asset Management agreements, for which IOR is the depository institution.

These are comprised of:

Deposits related to Asset management accounts	**2017**	**2016**
Deposits on demand	338,920	417,026
Time deposits		
Total	**338,920**	**417,026**

The item Due to customers also includes a deposit at the disposal of the Commission of Cardinals to support works of religion. As of the balance sheet date, this amounted to EUR 0.9m (2016: EUR 6.3m). The EUR 5.4m decrease was mainly due to the distribution of funds for charitable activities.

2.2 Subordinated liabilities

There are no subordinated liabilities recognized in this item.

ITEM 100 LIABILITIES – LEGATES

The item includes the deposits of the "Legates" amounting to EUR 47.0m (2016: 47.1m) as of 31 December 2017, comprised of 297 funds (2016: 293) donated to the Institute. The IOR has the burden, for a significant period of time, of fulfilling specific ecclesiastical functions or otherwise achieving purposes related to works of piety, apostolate and charity works, on the basis of its annual income.

ITEM 110 LIABILITIES – OTHER LIABILITIES

Other liabilities	2017	2016
Inheritances to be settled	4,023	6,384
Invoices to be received	4,748	4,515
Outstanding checks	659	1,070
Remunerations to be paid	1,055	914
Other sundry creditors	75	908
Funds for charitable contributions	3,353	3,220
Liabilities for guarantees issued and commitments towards third parties	1,699	1,699
Securities purchased not settled		
Total	**15,612**	**18,710**

The item "Inheritances to be settled" represents the property values of deceased donors pending resolution of inheritance issues.

The amount of EUR 1.7m (2016: EUR 1.7m) reported under" Liabilities for guarantees issued and commitments towards third parties" is due to guarantees in addition to the commitments to third parties to disburse funds whose cash out is uncertain (see paragraph 13.1 Guarantees and commitments).

Funds for charitable contributions are comprised of the Fund for Holy Masses and Fund for Missionary Activities.

Fund for Missionary Activities

The Fund for Missionary Activities is used to distribute contributions to congregations and institutions that operate missionary and charitable activities. The most common activities are the direct disbursement of contributions to student priests for the completion of university studies, financial aid for destitute persons or families (reported by Parishes or by individual priests), long-distance adoptions, specific help for missionary and charity work or aid to families that have lost everything as a result of natural disasters. It is mainly funded by small donations with a commitment to execute Missionary activities. Donations and distributions are recorded directly into the Fund's account. Distributions to the beneficiaries are approved by a Committee comprised of the Prelate, the Client Relationship Manager, and the Head of Operation, who took the place of the "Aggiunto al Direttore" in January 2018.

Fund for Holy Masses

The Fund for Holy Masses is used to distribute contributions to priests for Holy Masses. It is financed through small donations with a commitment to the Holy Masses. Donations and distributions are directly recorded into the Fund's account. Distributions to the priests are approved by a Committee comprised of the Prelate, the Client Relationship Manager, and the Head of Operation, who took the place of the "Aggiunto al Direttore" in January 2018.

The detail of Funds for charitable contributions is as follows:

Funds for charitable	2017	2016
A. Fund for Missionary Activities	**21**	**156**
1. Balance at 1 January	156	239
2. Donations received	97	86
3. Distributions for Missionary Activities	(232)	(169)
B. Fund for Holy Masses	**3,332**	**3,064**
1. Balance at 1 January	3,064	3,064
2. Donations received	445	83
3, Distributions for Holy Masses	(177)	(83)
Total	**3,353**	**3,220**

Distributions to beneficiaries are subject to strict internal policies approved by the Board.

It should be noted that the charitable activities of the Commission of Cardinals are made through a deposit included in item 20 of the liabilities.

ITEM 120 LIABILITIES – STAFF SEVERANCE FUND

10.1 Annual changes

	2017	2016
A. Opening balance	**6,993**	**6,788**
B. Increases		
B.1 Allocation for the year	519	534
B.2 Other changes	34	518
C. Decreases		
C.1 Benefits paid	(247)	(624)
C.2 Other changes	(122)	(223)
D. Closing balance	**7,177**	**6,993**

The Staff severance fund comprises indemnities paid to personnel when they leave the IOR.

The change in the fund balance is summarised as follows:

	2017	2016
Balance at 1 January	6,993	6,788
Current costs	447	459
Contribution by individuals	72	75
Transfers to benefit plan for pensions	-	(223)
Advances	(23)	(80)
Advances restitution	34	148
Consideration paid during the year	(224)	(544)
Actuarial (gain) loss of the year	(122)	370
Balance at 31 December	**7,177**	**6,993**

The actuarial assumptions used for the valuation of the Staff severance fund are the same as those used for the Benefit Plan Liability for pensions, described in Item 130 (a) Liabilities.

As defined by IAS 19, a sensitivity analysis was performed on the variation of the main actuarial assumptions included in the calculation model; these assumptions are:

- annual discount rate;
- annual rate of salary growth;
- annual mortality rate;
- probability of advances.

	Annual discount rate		Annual rate of salary growth		Annual mortality rate		Probability of advances	
Liabilities	**+0,50 p.p.**	**-0,50 p.p.**	**+0,50 p.p.**	**-0,50 p.p.**	**+0,50 p.p.**	**-0,50 p.p.**	**+0,025 p.p.**	**-0,025 p.p.**
	7,063	7,299	7,290	7,070	7,176	7,178	7,185	7,194

10.2 Other information

Please refer to the paragraphs regarding the accounting policies for more information on the calculation of employee termination indemnities.

The portion of employee gross salaries retained by the Institute is 1.5%.

No payments were made to the Vatican Pension Plan.

Funds were managed by the IOR Treasury department.

ITEM 130 LIABILITIES – ALLOWANCES FOR RISKS AND CHARGES

11.1 Detail by type

	2017	2016
1. Post employment benefits for pensions	133,335	121,088
2. Other allowances for risks and charges		
2.1 legal disputes		
2.2 staff expenses		
2.3 other	1,212	3,500
Total	**134,547**	**124,588**

11.2 Annual changes

	Provision for pension and similar obligations	Other provisions	Total
A. Opening balance	121,088	3,500	**124,588**
B. Increases			
B.1 Provision for the year	4,133		**4,133**
B.2 Time value changes			
B.3 Changes due to discount rate variations	11,198		**11,198**
B.4 Other changes			
C. Decreases			
C.1 Utilization in the year	(3,084)	(2,288)	**(5,372)**
C.2 Changes due to discount rate variations			
C.3 Other changes			
D. Closing balance	**133,335**	**1,212**	**134,547**

11.3 Pension plan liabilities defined benefit obligations

The Provision for pension and similar obligations fund comprises the Pension plan of the IOR employees.
More in detail, the changes in the Plan concern the following items:

	2017	2016
Opening balance	**121,088**	**108,338**
Current Service cost	703	607
Interest cost	1,685	2,031
New subscribers cost	1,649	
Contribution by individuals	96	93
Transfer from staff severance fund		223
Pensions paid during the year	(3,084)	(3,109)
Transfer out		
Actuarial (gain) loss of the year	11,198	12,905
Closing balance	**133,335**	**121,088**

The actuarial valuation of the defined benefit plan liability was performed using the following assumptions:

	2017	2016
Annual inflation rate	2.00%	2.00%
Annual discount rate	1.19%	1.43%
Annual rate for revaluation of pension	2.00%	2.00%
Annual rate of real increase salary	2.01%	2.35%

The Current Service Cost is the actuarial present value of benefits due to employees for services rendered during the period.

The Interest Cost is the increase in the present value of the obligation from the passage of time and it is proportional to the discount rate used in the assessment of the previous year's liabilities.

The Actuarial gain/loss is the change in the liability in the present year arising from:

- the effect of the differences between the previous actuarial assumptions and what has actually occurred;
- the effect of the changes in actuarial assumptions.

The results are recognized directly to Equity in a specific reserve named "Valuation reserves" "Post-employment benefit actuarial gain (loss) reserves" and the actuarial gain or loss is recorded in Other Comprehensive Income.

For Staff severance fund and Provisions for pensions and similar obligations, in 2017, the Institute recognized an actuarial loss of EUR 11.2m (2016: loss of EUR 13.3m) in Other Comprehensive Income. Consequently, change in the "Valuation reserves" (item 140 Equity) was a loss of EUR 57.1m (2016: EUR -46m); the increased loss compared to the prior year is due to the decrease in the discount rate to 1.19% in 2017 from 1.43% in 2016.

A total of 102 employees are active and contribute to the Pension plan (2016:102). A total of 74 former employees are in retirement and benefit from the plan (2016: 74).

As defined by IAS 19, a sensitivity analysis was performed on the variation of the main actuarial assumptions included in the calculation model; these assumptions are:

- annual discount rate;
- annual rate of salary growth;
- annual inflation rate;
- annual mortality rate.

Liabilities	Annual discount rate		Annual rate of salary growth		Annual inflation rate		Mortality rate	
	+0,50 p.p.	-0,50 p.p.	+0,50 p.p.	-0,50 p.p.	+0,50 p.p.	-0,50 p.p.	+0,025 p.p.	-0,025 p.p.
	120,280	145,756	132,813	131,391	145,704	120,211	131,717	132,471

11.4 Other information

Please refer to the paragraphs regarding the accounting policies for more information on the calculation of the pension fund.

The portion of employee gross salaries retained by the Institute is 6%.

No payments were made to the Vatican Pension Plan.

Funds were managed by the IOR Treasury department.

11.5 Other provisions

As of 31 December 2017 the Institute, based on the analysis carried out until now with the help of legal advisors, has almost reached the final estimate of the outstanding liability for which it has already recorded the cash outflow. Pending the formal and definitive conclusion of this issue, IOR has maintained on its books a residual provision of EUR 1.2m, included in item 130 b "Provisions for risks and charges" on line b "Other Funds" of the Balance Sheet. As this represents an estimate based on critical assumptions, upon the conclusion of future events, actual results may differ from what is expected.

The relative content of the item was explained in the paragraph 1.1.4 Other aspects - Critical accounting estimates and judgements, Part 1 Accounting policies.

ITEM 160 170 EQUITY – RESERVES

12.1 Capital

Capital, as a separate component of Equity, represents a permanent endowment that cannot be reduced or distributed, except in case of cessation or liquidation of the entity.

During 2017, no changes were recorded in Capital balance, amounting to EUR 300m.

Securities and liquid funds made up the Capital; in detail, deposits to APSA, other liquid assets, supranational bonds and governative bonds with high quality credit rating.

12.2 Reserves

The equity balance is comprised of two different reserves, Available and Unavailable reserves.

Unavailable Reserves are earning reserves designed to further strengthen the Institute's Equity and long-term stability.

Available Reserves are earning reserves representing earnings that could potentially fulfill a "stabilization" function, subject to a resolution of the Commission of Cardinals.

During 2017, no changes were recognized in Unavailable Reserves, amounting to EUR 100m, and Available Reserves, amounting to EUR 282m.

Unavailable reserves are comprised of securities, properties and precious metals. In detail, these reserves are comprised of gold bars, medals and coins, investment in subsidiary (S.G.I.R. S.r.l.), real estate properties and liquid financial instruments traded on regulated markets.

The Available Reserve is comprised of securities, representing liquid financial instruments traded on regulated markets.

13 Additional information

13.1 Guarantees and commitments

	2017	2016
1) Financial guarantees given to		
a) Banks		
b) Customers	27	42
2) Commercial guarantees given to		
a) Banks		
b) Customers		
3) Irrevocable commitments to disburse funds to		
a) Banks		
b) Customers		
i) cash out certain		
ii) cash out uncertain	4,000	4,000
4) Underlying commitments on credit derivatives: sales of protection		
5) Assets pledged as collateral for third-party commitments		
6) Other commitments		
Total	**4,027**	**4,042**

At the balance sheet date, the Institute has a commitment of EUR 4m of uncertain use issued in favor of third parties.

As at 31 December 2017, the IOR has one guarantee issued before the year 2000 and covered by assets held in custody.

No new guarantees were issued in 2017.

The guarantees were initially recognized at their nominal value, which is their fair value. In subsequent periods, the guarantees are reported at the amount determined in accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets".

13.4 Asset Management and Brokerage on behalf of third parties

	2017	2016
1. Trading on behalf of customers		
(a) purchases		
(i) settled	122,935	129,087
(ii) to be settled		
(b) sales		
(i) settled	93,901	84,530
(ii) to be settled		
2. Portfolio management (assets management)		
(a) individual	2,957,652	3,110,929
(b) collective		
3. Custody and administration of securities		
(a) third party security held in deposit: related to depositary bank activities (excluding portfolio management)		
(i) security issued by the entity that prepare the financial statement		
(ii) other securities		
(b) third party securities held in deposit: other (excluding portfolio management)		
(i) security issued by the entity that prepare the financial statement		
(ii) other securities		
(c) third party securities deposited with third parties	474,594	554,763
(d) proprietary portfolio securities deposited with third parties	2,380,889	2,508,160
4. Other operations		

Assets under Management consist mainly of client-owned securities held at the IOR for management purposes. Investment decisions are made by the IOR on the basis of portfolio management mandates signed with its clients.

Assets under Management agreements are valued using the mark-to-market method. They include the total value of portfolios as well as, liquid and term deposits. Accruals are also included, both on securities and on liquid and term deposits. The IOR is the depository of liquid and term deposits, amounting to EUR 338.9m (2016: EUR 417.2m), as disclosed in item 20 Liabilities “Due to customers”.

Assets under Custody mainly include client-owned securities held at the IOR for custodial purposes. The clients make all investment decisions and the IOR has no discretionary power to manage these assets, provided that such decisions are in accordance with the role and mission of the Institute.

Assets under custody agreements are also valued based on current bid prices, using the mark-to-market method. They also include accruals on interest to be received on debt securities.

PART 3. INFORMATION ON THE INCOME STATEMENT

ITEM 10 INCOME STATEMENT – INTEREST AND SIMILAR INCOME

1.1 Interest income and similar income: detail

	Debt securities	Loans	Other transactions	2017	2016
1. Financial assets held for trading	19,944			**19,944**	**22,574**
2. Financial assets available for sale					
3. Financial assets held to maturity	10,522			**10,522**	**15,217**
4. Due from banks	-	1,393		**1,393**	**1,615**
5. Due from customers	-	304		**304**	**426**
6. Financial assets carried at *fair value*					
7. Hedging derivatives					
8. Other assets					
Total	**30,466**	**1,697**		**32,163**	**39,832**

In 2017 the Institute recorded a general decrease in all items related to interest margin, both income and expense, which consequently led to a net reduction in the Interest Margin.

Interest and similar income accrued during the year in positions classified as impaired (other than those recorded in the item 130 Income Statement "Net losses/reversal on impairment") at the balance sheet date amounted to EUR 342,000. They were directly deducted from line 5 in the table above.

ITEM 20 INCOME STATEMENT – INTEREST AND SIMILAR EXPENSES

1.4 Interest and similar expenses: detail

	Payables	Securities	Other transactions	2017	2016
1. Due to Public Entities					
(i) Public Authorities					
(ii) Foreign Public Authorities					
(iii) International and Regional Organizations					
2. Due to banks	(11)			**(11)**	**(52)**
3. Due to customers	(3,190)			**(3,190)**	**(3,117)**
4. Outstanding securities					
5. Financial liabilities held for trading					
6. Financial liabilities designated at *fair value through profit and loss*					
7. Other liabilities and funds					
8. Hedging derivatives					
9. Due to other subjects					
Total	**(3,201)**			**(3,201)**	**(3,169)**

Interest income decreased due to the impact of lower interest rates determined by the European Central Bank in 2014, 2015 and 2016, and the expiration of many positions with higher interest rates.

Interest expense recorded the same amount of the previous year.

ITEM 40 INCOME STATEMENT – FEE AND COMMISSION INCOME

2.1 Fee and commission income: detail

	2017	2016
a) Guarantees given/received	1	1
b) Credit derivatives		
c) Administration, brokerage and consultancy services:		
1. trading in financial instruments	711	654
2. trading in currencies		
3. portfolio management		
3.1 individual	12,540	12,483
3.2 collective		
4. Custody and administration of securities	93	113
5. Custodian bank		
6. Securities placement		
7. Receipt and transmission of orders activity		
8. Consulting		
8.1 investments		
8.2 financial structure		
9. Distribution of third-party services		
9.1 portfolio management		
9.1.1 individual		
9.1.2 collective		
9.2 insurance products		
9.3 other products		
d) collection and payment services	2,226	2,196
e) *servicing* of securitization operations		
f) factoring services		
g) rate and tax collection office services		
h) multilateral trading systems management		
i) current account keeping and management	340	369
j) other services	16	21
Total	**15,927**	**15,837**

The Fee and Commission income recorded the same amount of the previous year.

2.2 Fee and commission income: distribution channels of products and services

All the IOR products and services are offered at IOR locations in Vatican City State.

ITEM 50 INCOME STATEMENT – FEE AND COMMISSION EXPENSE

2.3 Fee and commission expense: detail

	2017	2016
a) Guarantees given/received		
b) Credit derivatives		
c) Administration, brokerage and consultancy services:		
1. trading in financial instruments	(114)	(83)
2. trading in currencies		
3. portfolio management		
3.1 own portfolio		
3.2 third-party portfolio		
4. Custody and administration of securities	(1,434)	(1,613)
5. Placement of financial instruments		
6. Sales of financial instrument, products and services through other outlets		
d) Collection and payment services	(648)	(761)
e) Administration and management of current accounts	(1,427)	(571)
f) Other services	(1)	(1)
Total	**(3,623)**	**(3,029)**

The increase in Fee and commission expense was mainly due to the fee and commissions charged by correspondent banks on current accounts of the Institute as charges for the management of liquidity (+145%); while the custody and administration fees for securities slightly decrease.

ITEM 70 INCOME STATEMENT – DIVIDENDS AND SIMILAR INCOME

3 Dividends and similar income: detail

	2017		2016	
	Dividends	Income from UCI	Dividends	Income from UCI
A. Financial assets held for trading	508	400	860	812
B. Financial assets available for sale	237		435	
C. Financial assets carried at *fair value through profit and loss*				
D. Investment in subsidiaries				
Total	**745**	**400**	**1,295**	**812**

Dividends received in 2017 for financial assets held for trading were EUR 0.9m (2016: EUR 1.7m), recording a strong decrease, in line with the reduction of equites held in the category.

Of this, income from UCI units, which relates to dividends distributed by investment funds, decreased by 50%.

In 2017, the Institute received dividends of EUR 237,000 from investment securities recorded as financial assets available for sale (2016: EUR 435,000).

4. Net income from trading activities: detail

	2017				
	Gains (A)	Profit from trading activities (B)	Losses (C)	Losses from trading activities (D)	Net income [(A+B) - (C+D)]
1. Financial assets held for trading					
1.1 Debt securities	7,886	2,267	8,673		**1,480**
1.2 Equity securities	2,045	1,749	281		**3,513**
1.3 UCI units	258	134	1,092		**(700)**
1.4 Loans					
1.5 Other		3			**3**
2. Financial liabilities held for trading					
2.1 Debt securities					
2.2 Payables					
2.3 Other					
3. Financial assets and liabilities: exchange differences	86	3,727	582		**3,231**
4. Derivatives					
4.1 Financial derivatives					
- On debt securities and interest rates					
- On equity securities and stock indices					
- On currencies and gold					
- Other					
4.2 Credit derivatives					
Total	**10,275**	**7,880**	**10,628**		**7,527**

	2016				
	Gains (A)	Profit from trading activities (B)	Losses (C)	Losses from trading activities (D)	Net income [(A+B) - (C+D)]
1. Financial assets held for trading					
1.1 Debt securities	6,167	1,429	6,041		**1,555**
1.2 Equity securities	1,603		1,509		**94**
1.3 UCI units	1,693		14,445		**(12,752)**
1.4 Loans					
1.5 Other		126			**126**
2. Financial liabilities held for trading					
2.1 Debt securities					
2.2 Payables					
2.3 Other					
3. Financial assets and liabilities: exchange differences	1,529	470	5		**1,994**
4. Derivatives					
4.1 Financial derivatives					
- On debt securities and interest rates					
- On equity securities and stock indices					
- On currencies and gold					
- Other					
4.2 Credit derivatives					
Total	**10,992**	**2,025**	**22,000**		**(8,983)**

Below is a summary of the net trading results in 2017 compared to 2016.

In 2017, debt securities recognized a gain of EUR 1.5m compared to a gain of EUR 1.6m in 2016. Realized gain from trading activity was EUR 2.3m compared to a gain of EUR 1.4m in 2016, and the unrealized loss was EUR 787,000 compared to a gain of EUR 126,000 in 2016.

In 2017, equity securities recognized a gain of EUR 3.5m compared to a gain of EUR 94,000 in 2016. A realized profit of 1.7m was recognized compared to no realized profit (loss) in 2016, while unrealized gain was EUR 1.8m, compared to EUR 94,000 in 2016.

In 2017, UCI units recognized a loss of EUR 700,000 compared to a gain in 2016 of EUR 12.8m. A realized profit of 134,000 was recorded in 2017 compared to no realized gain in 2016, while unrealized loss was EUR 834,000 compared to an unrealized gain of EUR 12.8m in 2016.

Line 1.5 "Financial assets held for trading: other" includes gains (losses) from currency trade, gold and other precious metals, recognizing a gain of EUR 3,000 in 2017 compared to EUR 126,000 in 2016 (realized).

"Financial assets and liabilities: exchange differences" recognized a gain of EUR 3.2m compared to a profit of EUR 2m in 2016, comprised of EUR 3.7m realized profit in 2017 compared to EUR 470,000 in 2016 and unrealized loss of EUR 496,000 in 2017 compared to profit of EUR 1.5m in 2016.

ITEM 100 INCOME STATEMENT - PROFIT (LOSS) ON DISPOSAL OR REPURCHASE

6. Profit (loss) on disposal or repurchase: detail

	2017			2016		
	Profit	Losses	Net income	Profit	Losses	Net income
Financial assets						
1. Due from banks						
2. Due from customers						
3. Financial assets available for sale						
3.1 Debt securities						
3.2 Equity securities	1,386		1,386	1,518	(19)	1,499
3.3 UCI units						
3.4 Loans						
4. Financial assets held to maturity						
Total assets	**1,386**		**1,386**	**1,518**	**(19)**	**1,499**
Financial liabilities						
1. Due to banks						
2. Due to customers						
3. Outstanding securities						
Total liabilities						

ITEM 130 INCOME STATEMENT – NET LOSSES/REVERSAL ON IMPAIRMENT

8.1 Net impairment losses on loans: detail

	Value adjustments (1)			Write-backs (2)					
	Specific		Port-folio	Specific		Portfolio			
	Derecognition	Other		A	B	A	B	2017 (1)+(2)	2016 (1)+(2)
1. Due from banks									
- Loans									
- Debt securities									
2. Due from customers									
Purchased impaired loans									
- Loans									
- Debt securities									
Other receivables									
- Loans	(45)	(725)			259		119	**(392)**	**353**
- Debt securities									
Total	**(45)**	**(725)**			**259**		**119**	**(392)**	**353**

8.2 Net impairment losses on financial assets available for sale: detail

	Value adjustments (1)		Write-backs (2)			
	Specific		Specific			
	Derecognition	Other	A	B	2017 (1)+(2)	2016 (1)+(2)
1. Debt securities						
2. Equity securities						**(148)**
3. UCI units						
4. Loans to banks						
5. Loans to customers						
Total						**(148)**

8.4 Net impairment losses on other financial assets: detail

	Value adjustments (1)			Write-backs (2)					
	Specific		Port-folio	Specific		Portfolio			
	Derecognition	Other		A	B	A	B	2017 (1)+(2)	2016 (1)+(2)
1. Guarantees given									**(138)**
2. Credit derivatives									
3. Commitments to lend funds									
4. Other operations									
Total									**(138)**

9.1 Personnel expenses: detail

	2017	2016
A. Staff		
1. Wages and salaries	(5,022)	(5,078)
2. Social security charges		
3. Termination indemnities		
4. Supplementary benefits	(630)	(630)
5. Provisions for termination indemnities	(447)	(459)
6. Provisions for post employment benefits		
(a) defined contribution plans		
(b) defined benefit plans	(4,037)	(2,638)
7. Payments to external pension plans		
(a) defined contribution plans		
(b) defined benefit plans		
8. Other benefits in favor of employees	(241)	(546)
B. Current Personnel with contracts pursuant to ex art. 10 (1)		
1. letter (b)		
2. letter (c)		
3. letter (d)		
C. Fees and charges for:		
1. Board of Superintendence	(668)	(504)
2. Directorate	(308)	(299)
3. *Revisori*	(88)	(91)
D. Early retirement cost		
E. Recovery of expenses for employees seconded to other entities		
F. Reimbursement of expenses for employees of the institutions and organizations of the Holy See and the Vatican City State placed at the Institute.		
Total	**(11,441)**	**(10,245)**

9.2 Average number of employees by categories

Type	Total	Managers	Officials	Staff
Average number	102	4	5	93

Reimbursement of expenses for employees of the institutions and organizations of the Holy See and the Vatican City State placed at the Institute.

9.3 Post employment defined benefit plans: costs and revenues

Post employment defined benefit plans: costs	**2017**	**2016**
Current Service cost of internal Pension Plan	(703)	(607)
Interest cost of internal Pension Plan	(1,685)	(2,031)
New positions cost	(1,649)	
Post employment costs: contribution to Vatican Pension Plan	(630)	(630)
Total Costs	**(4,667)**	**(3,268)**
Post employment defined benefit plans: revenues		
Total	**(4,667)**	**(3,268)**

9.5 Professional service expenses: detail

	2017	**2016**
A. Professional services expenses		
1. Legal services	(1,940)	(2,437)
2. Directional consultants	(149)	(718)
3. Technical consultants	(200)	(288)
4. Operational consultants	(196)	(342)
5. Translational services	(49)	(56)
B. Expenses related to works contract		
1. ex art. 10 (1) (a)		
2. ex art. 11 (1)		
C. Expenses related to outsourcing contracts		
D. Expenses related to independent auditors	(121)	(121)
Total	**(2,655)**	**(3,962)**

9.6 Other administrative expenses: detail

	2017	**2016**
1. Software maintenances	(1,688)	(1,441)
2. Other maintenances	(440)	(800)
3. Information providers	(376)	(379)
4. AIF contribution	(200)	(346)
5. Other expenses	(1,927)	(1,913)
Total	**(4,631)**	**(4,879)**

ITEM 160 INCOME STATEMENT – NET PROVISION FOR RISKS AND CHARGES

Detailed information is provided in Item 130 (b) Liabilities.

ITEM 170 INCOME STATEMENT – NET VALUE ADJUSTMENTS TO/RECOVERIES ON TANGIBLE ASSETS

11. Net value adjustments to/recoveries on tangible assets: detail

	2017				2016			
	Depre-ciation (a)	Impairment losses (b)	Recoveries (c)	Net income (a+b-c)	Depre-ciation (a)	Impairment losses (b)	Recoveries (c)	Net income (a+b-c)
A. Tangible assets								
A.1 Owned assets								
- Functional use	(69)			(69)	(83)			(83)
- For investment								
A.2 Acquired under finance lease								
- Functional use								
- For investment								
Total	**(69)**			**(69)**	**(83)**			**(83)**

ITEM 180 INCOME STATEMENT – NET VALUE ADJUSTMENTS TO/RECOVERIES ON INTANGIBLE ASSETS

12. Net value adjustments to/recoveries on intangible assets: detail

	2017				2016			
	Depre-ciation (a)	Impairment losses (b)	Recoveries (c)	Net income (a+b-c)	Depre-ciation (a)	Impairment losses (b)	Recoveries (c)	Net income (a+b-c)
A. Intangible assets								
A.1 Owned assets								
- Generated internally by the Institute								
- Other	(489)			(489)	(683)			(683)
A.2 Acquired under finance lease								
Total	**(489)**			**(489)**	**(683)**			**(683)**

ITEM 190 INCOME STATEMENT – OTHER OPERATING INCOME (EXPENSE)

13.1 Other operating income (expense): detail

	2017	2016
A. Income	**459**	**736**
Extraordinary income	459	558
Recovery of amounts for gold and precious metals		178
Closure of past years issue		
B. Expenses	**(295)**	**(729)**
1. Operating losses	(278)	(715)
2. Extraordinary expenses	(5)	(14)
3. Impairment of amounts for gold and precious metals	(12)	
Total	**164**	**7**

15. Net result of fair value valuation of tangible and intangible assets: detail

2017	Revaluations (a)	Impairment (b)	Exchange differences Positive (c)	Exchange differences Negative (d)	Net income (a-b+c-d)
A. Tangible assets					
A.1 Owned assets					
- Functional use					
- Held for investment	136	14			122
A.2 Acquired under finance lease					
- Functional use					
- Held for investment					
B. Intangible assets					
B.1 Owned assets					
B.1.1 Generated internally by the Institute					
B.1.2 Other					
B.2 Acquired under finance lease					
Total	**136**	**14**			**122**

2016	Revaluations (a)	Impairment (b)	Exchange differences Positive (c)	Exchange differences Negative (d)	Net income (a-b+c-d)
A. Tangible assets					
A.1 Owned assets					
- Functional use					
- Held for investment	136	53			83
A.2 Acquired under finance lease					
- Functional use					
- Held for investment					
B. Intangible assets					
B.1 Owned assets					
B.1.1 Generated internally by the Institute					
B.1.2 Other					
B.2 Acquired under finance lease					
Total	**136**	**53**			**83**

PART 4. INFORMATION ON COMPREHENSIVE INCOME

	2017			2016		
	Gross amount	Income tax	Net amount	Gross amount	Income tax	Net amount
10. Profit (loss) for the year	**31,934**		**31,934**	**36,001**		**36,001**
Other comprehensive income that may not be reclassified to the income statement						
20. Tangible assets						
30. Intangible assets						
40. Defined benefit plans	(11,076)		(11,076)	(13,275)		(13,275)
50. Non current assets held for sale						
60. Share of valuation reserves connected with investments carried at equity						
Other comprehensive income that may be reclassified to the income statement						
70. Hedges of foreign investment						
(a) fair value changes						
(b) reclassification to the income statement						
(c) other changes						
80. Foreign exchange differences						
(a) fair value changes						
(b) reclassification to the income statement						
(c) other changes						
90. Cash flow hedges						
(a) fair value changes						
(b) reclassification to the income statement						
(c) other changes						
100. Financial assets available for sale						
(a) fair value changes	1,662		1,662	(1,838)		(1,838)
(b) reclassification to the income statement						
- impairment losses				148		148
- gains (losses) from disposals				(2,589)		(2,589)
(c) other changes						
110. Non current assets held for sale						
(a) fair value changes						
(b) reclassification to the income statement						
(c) other changes						
120. Share of valuation reserves connected with investments carried at equity:						
(a) fair value changes						
(b) reclassification to the income statement						
- impairment losses						
- gains (losses) from disposals						
(c) other changes						
130. Total other comprehensive income	**(9,414)**		**(9,414)**	**(17,554)**		**(17,554)**
Total Comprehensive Income (item 10 + item 130)	**22,520**		**22,520**	**18,447**		**18,447**

ATTACHMENTS

A.1 Disclosure concerning the fees of the independent auditors and services other than auditing

During 2017, the IOR did not pay fees to the companies belonging to the network of the audit firm Deloitte & Touche S.p.A. with the exception of those related to the audit of the annual accounts amounting to EUR 121,000.

The fees due are those contractually agreed, inclusive of any indexation and reimbursement of expenses calculated as a forfeit. Fees do not include out-of-pocket expenses or taxes.

A.2 Exchange rates as of the balance sheet date

The balances at year-end, denominated in foreign currencies, are measured at the exchange rates observed by the European Central Bank on the last working day of the year (in 2017: 29 December).

For the other currencies, the rates used are those provided by infoproviders on the same date.

For the 2017 financial statements, the rates were determined as follows:

Currency		**2017**	**2016**
U.S. Dollars	USD	1.1993	1.0926
Swiss Francs	CHF	1.1702	1.0814
Canadian Dollars	CAD	1.5039	1.5171
English Pounds	GBP	0.8872	0.7380
Australian Dollars	AUD	1.5346	1.4990
Japanese Yen	JPY	135.01	131.66
Czech Crowns	CZK	25.535	27.029
Danish Crowns	DKK	7.4449	7.4625
Hungarian Forints	HUF	310.33	313.15
Norwegian Crowns	NOK	9.6723	9.6160
Polish Zloty	PLZ	4.1770	4.2400
Swedish Crowns	SEK	9.8438	9.1878
Brazilian Reais	BRE	3.9729	4.2590
South African Rand	ZAR	14.8054	16.8847
Hong Kong Dollars	HKD	9.3720	8.4685
South Korean Won	KRW	1.224.94	1.284.79
Singapore Dollars	SGD	1.6024	1.5449
New Zealand Dollars	NZD	1.6850	1.5959

A.3 Date of authorisation for issue

The financial statements were presented and authorised for issuance by the Directorate on 23 March 2018 and approved by the Board of Superintendence on 24 April 2018.

PART 5. INFORMATION ON RISKS AND HEDGING POLICIES

5.1 Introduction

The Institute's policies and procedures for the management and monitoring of risks arising from investments decisions, are summarized in the following paragraphs, with a focus on the parties involved and their responsibilities. The Institute considers it appropriate:

a) to assign risk measurement functions and risk integrated control to a specific department, headed by the Risk Management department;

b) to assign the functions dedicated to the definition of operating limits, the authorization of possible overruns or payment requests within assigned limits, to the appropriate Risk Committee.

Other bodies of the Institute are involved and assigned with different tasks in risk management and monitoring, such as the Board of Superintendence, Directorate, Internal Audit department, Treasury department, Compliance.

This structure is based on the Vatican laws and rules and requirements provided by the Financial Information Authority (AIF) for a compliant internal audit system, as defined by Regulation No.1/2015 on "Prudential Supervision of Entities Carrying out financial activities on a professional basis ("Regolamento n.1"), implementing Title III of the Law introducing norms of "Transparency, Supervision and Financial Intelligence" no. XVIII issued on 8 October 2013 ("Law no. XVIII").

The Risk Management function is an independent structure from the risk-taking functions, reporting directly to the Directorate and with functional reporting also to the Board of Superintendence. The following paragraphs set out the rules of the different organizational structures and the governing bodies involved in the monitoring and managingement of risks.

5.1.1 Duties and responsibilities of bodies involved

The Institute bodies involved in various capacities in the management and monitoring of risk relating to investment decisions are the following:

- Board of Superintendence;
- Directorate;
- Risk Committee;
- Risk Management Department;
- Compliance Department;
- Internal Audit Department;
- Head of Treasury Department;

5.1.1.1 Board of Superintendence

The Board of Superintendence is responsible for defining the strategic guidelines, the Risk Appetite and general policies for risk management. The Board of Superintendence can request the Directorate to update the guidelines for the measurement and assessment of risks and periodically monitors the performance of risks and compliance with the limits established on the basis of the information produced by the Risk Management function and the Risk Committee.

5.1.1.2 Directorate

The Directorate establishes the overall strategies, general policies and guidelines set forth by the Board of Superintendence and any amendments thereto, the risk management and monitoring methodologies and their implementation and integration proposed by the Risk Committee, and the general structure of market and credit operational limits (counterparty risk and issuer risk), consistently with the overall Risk Appetite.

The Directorate also establishes periodically, based on the proposal of the Risk Committee, the limits granted to new trading partners.

The Directorate monitors the risk exposure on a daily basis, through reports produced by the Risk Management department, and is informed promptly by the department when operational limits have been exceeded and can request an emergency meeting of the Risk Committee.

When operational limits are exceeded, based on a proposal from the Risk Committee, the Directorate determines the way in which the overrun may be managed:

- the Directorate can authorize the overrun specifying the period for which the authorization is granted;
- the Directorate can ask the head of the operating area involved for a recovery plan to be established. The Directorate then authorizes the plan, or can ask for recovery in different ways and/or in different periods than the recovery period proposed.

5.1.1.3 Risk Committee

A Risk Committee has been established by the Directorate and chaired by Head of Risk Management department with the aim:

- to propose a Risk Appetite Framework and management and control methodologies and all subsequent amendments thereof, in compliance with the general limits set up by RAF;
- to propose to the Directorate the general structure of market and credit operational limits (counterparty risk and issuer risk);
- to propose periodically to the Directorate credit limits granted to the new trading partners, in compliance with the general limits defined in the RAF;
- to periodically review the Institute's risk trend, with specific focus on the most relevant events or those with the greatest impact;
- in case of an emergency meeting, where operational limits have been exceeded, to express an opinion to the Directorate on the authorization for exceeding limits, or on the recovery plan arrangements.

The organizational aspects of the Risk Committee are disclosed in an appropriate regulation.

5.1.1.4 Risk Management Department

The Institute's Risk Management department:

- presents to the Risk Committee issues related to the Institute's exposure to market, credit, liquidity, operational and reputational risks, proposing methodologies, instruments and processes for the management of those risks;
- is responsible for the implementation, validation and maintenance of an adequate risk exposure control system and its performance;
- on a daily basis, observes the market, credit and liquidity risks and trading activity performance, preparing specific reports for the Board, the Directorate and the head of Treasury Department;
- monitors the compliance with the risk indicators outlined in the Risk Appetite Framework (RAF) approved by the Board of Superintendence, preparing specific reports;
- monitors the adherence to operational limits in the Institute's trading activity, promptly informing the Directorate and the head of Treasury Department of any overruns. When limits are exceeded, it can request an emergency meeting of the Risk Committee;
- calculates capital requirements in compliance with legal requirements.

5.1.1.5 Compliance Department

The IOR Compliance Department, in accordance with AIF Regulation No. 1, oversees, using a risk-based approach, management of the risk of non-compliance in corporate activity, ensuring that internal procedures are suitable to prevent such risk.

In particular, it is responsible for managing the risk of non-compliance with the most important regulations, such as those relating to financial activity and brokerage, anti-money laundering, and management of conflicts of interest, ensuring that the internal procedures are suitable to mitigate these risks.

As regulated by Article 29 of Regulation No. 1, in order to achieve its mission, the Compliance Department:

- remains current on the rules applicable to the Institute and its activities and measures/assesses the impact of any changes on existing processes and internal procedures;
- verifies compliance with external regulatory requirements and self-regulation;
- proposes organizational and procedural changes that ensure adequate supervision of the risk of non-compliance with identified rules;
- monitors effectiveness of the suggested organizational changes for prevention of the risk of non-compliance;
- prepares direct information flows for the Institute's governance bodies and for the other concerned functions/structures;

- provides advice and assistance to the Institute's governance bodies for all matters in which the non-compliance risk is relevant as well as collaboration in training personnel on the provisions applicable to their activities.

5.1.1.6 Internal Audit Department

The Institute's Internal Audit department verifies through the audit plan:

- the adherence to risk management procedures as established by the Board of Superintendence and by the Directorate, based on a proposal from the Risk Committee;
- the adequacy of the risk monitoring tools and procedures related to the Institute's investment decisions.

5.1.1.7 Head of Treasury Department

- Defines the operating investment decisions to be made on financial markets, ensuring consistency with the strategic goals and predetermined limits.
- Requests revisions to the assigned operational limits, or the authorization to engage with new counterparties, subject to the review of the Risk Committee.
- Defines, within the limits of the authority granted, the necessary corrective actions to restore the defined risk/return profile.

5.1.2 Risk culture and further developments

The Institute is involved in a complete overview of its current financial, credit, liquidity, reputational and operational risks management programs. This involves the strengthening of the second level control functions (Risk Management and Compliance), through the review of risk measurement and assessment systems and the adaptation to the most common market practices, which includes preparation for the introduction of the new accounting standard IFRS9 for the classification and measurement of financial instruments.

The approval of a Risk Appetite Framework integrated in the activities of daily risk management allows for the development and dissemination of a risk culture, while the consolidation of the role of the Risk Committee has contributed to maintaining a high level of attention from the management.

An ad-hoc e-learning platform for trainings was delivered by the Institute to capture the specificities of the Institute and the current regulatory framework, in particular, in the anti-money laundering and combating the financing of terrorism. External training activities are planned for specific areas, in particular, in the case of regulatory changes or in order to provide new skills.

5.2 Credit risk

Format and content of information on credit risk and related hedging policies

5.2.1 General aspects

Credit risk rises from the possibility that counterparties may not honour their commitments. Depending on the nature of those commitments, the Institute's credit risk may be divided in two categories:

a) credit risk arising from the Institute's investment and trading activity for their own account and on behalf of its clients. Credit risk represents the risk that a counterparty may not fulfill its contractual obligations related to a transaction concerning financial instruments. This risk may be classified into three categories:

1) cash risk (e.g. deposits);
2) issuer risk (e.g. bond purchases);
3) counterparty risk, mainly generated by the operations in Delivery versus Payment (e.g. term operations, repos).

b) credit risk arising from loans to customers, classified in the financial statements as "Due from customers"; within this risk category, the Institute considers it appropriate not to measure this risk because:

- the item is not material when compared to total assets;
- the exposure is limited to Catholic congregations and Vatican employees, both of which have low risk categories by their nature;

- credits are usually accompanied by guarantees: securities, asset management or, for the Institute employees, post employment benefits.

It is to be mentioned that the Institute is not authorized by the Autorità di Informazione Finanziaria to carry out the activity of "lending" (cfr. art. l (l) (b) of the Law n. XVIII and art. 3 (24) (b) of the Regulation No. l), as credit activities on its own. However, it is authorized to make "advances" that is to disburse funds to its clients and to a limited extent following guarantee of future income (such as, for example, in the case of the advance of salary or pension paid by the Holy See or the Governatorato of Vatican City) or guaranteed by financial assets of the same amount deposited by the clients at the Institute.

In general, the main sources of credit risk derive from the investment in bonds, mainly issued by government, financial and corporate "Investment Grade" rating agencies and by deposits with banks. In consideration of the general level of interest rates and yields offered, the strategy in 2017 was to focus more on issuers of good credit standing, favoring both issues with medium-short maturity and variable-rate or inflation-linked securities.

At the end of 2017, the bond securities portfolio amounted to EUR 2.3bn with an average duration of 1.372 years and high credit standing (99.6% investment grade). The portfolio is composed of governament bonds issued by major European countries (core and peripheral), as well as financial and corporate bonds.

Additional details on the bond portfolio composition are provided in the next paragraphs.

5.2.2 Credit risk management policies

5.2.2.1 Organizational aspects

The Treasury Department is responsible for the management and monitoring of credit risks over trading activity and collections of amounts due from clients. The Treasury Department is qualified to assume credit risk in compliance with operational limits. Particularly, the process of risk assumption involves the following:

- the Director General delegates the assumption of credit risks to the Treasury Department, within a predetermined amount, type and counterparty;
- the Treasury Department assumes credit risk in its operations in compliance with its defined limits. The assumption of credit risk for amounts greater than the predetermined limit assigned to the department requires the authorisation of the Director General;
- the Risk Committee supports the Director General in establishing a system of credit risk management and monitoring, defining operational limits, analyzing any overruns and in evaluating authorisations of limits exceeded;
- the Risk Management Department, on a daily basis, monitors compliance with operational limits, promptly reporting to the Directorate any unauthorized overruns.

5.2.2.2 Management, measurement and control systems

Credit risk monitoring activity is delegated to the Risk Management Department, applying the Institute's specific-methodology, validated by the Risk Committee and approved by the Director General.

This methodology provides, in particular, for the definition of:

- a set of determined counterparties with which the Treasury department is allowed to engage with. For each counterparty, the type of risk that the Institute can assume and the maximum amount of exposure are defined;
- credit risk quantification criteria for each financial instrument, distinguishing between counterpart risk, issuer risk and cash risk;
- add-on quantification criteria to be applied to all contracts with future settlement, diversified by maturity and margining practices.

Concerning the maximum amount of exposure to each counterparty, the methodology provides for the use of an internal rating, defined by the characteristics of the counterparty, the rating from International Rating Agencies (Moody's, S&P, Fitch) and credit spread level quoted in the market (spread on Credit Default Swaps). The use of the credit default swaps spread enables prompt updating of the internal rating and their credit maximum exposure when the market shows signs of difficulties with a determined issuer before these difficulties can lead to a change of the counterparty's rating.

In addition to the limits defined above, the Board of Superintendence defined other limits at trading portfolio level based on a sensitivity spread, distinguishing between government and corporate issuer. The impact of this stress test at the closing date of this financial statements amount respectively to EUR 20.4m and EUR 16.1m.

5.2.2.3 Credit risk mitigation techniques

Currently, the Institute has no offsetting agreements in place with financial counterparties and does not operate in the credit derivatives market.

5.2.2.4 Non-performing financial assets

For amounts due from clients, an internal monitoring system assists the Directorate in determining if there is objective evidence of the impairment of loans, based on the following criteria established by the Institute:
- default in contractual payments of both capital and interest;
- delays in payments due to liquidity problems of customers;
- deterioration in the value of the guarantees provided.

The IOR has also issued guarantees requested by customers covered by assets held in custody, which are disclosed on paragraph 13.1 Part 3.

5.2.3 Credit quality

As disclosed in AIF Circular, the use of the term "exposures" includes equity securities and UCI units while the use of the term "credit exposures" excludes equity securities and UCI units.

1 Performing and non-performing credit exposures: amounts, adjustments, changes, economic and geographical detail

1.1 Detail of credit exposures by portfolio classification and credit quality (book values)

	Bad loans	Unlikely to pay	Non performing past due exposures	Performing past due exposures	Other performing exposures	Total
1.Financial assets available for sale						
2.Financial assets held to maturity					246,168	246,168
3.Due from banks					473,386	473,386
4.Due from customers		6,969			18,453	25,423
5.Financial assets carried at *fair value*						
6.Financial assets being disposed						
Total 2017		**6,969**			**738,007**	**744,977**
Total 2016		**7,469**	**764**	**71**	**1,223,033**	**1,231,337**

Note: *There are no forborne exposures.*

At the closing date of these financial statements there were not performing past due exposures. Based on the analysis of debtors, there was no objective evidence of potential insolvency of the customer and no impairment loss was recognized.

Bad loans are totally impaired.

1.2 Detail of credit exposures by portfolio classification and credit quality (gross and net values)

	Non-performing assets			Performing assets			
	Gross exposure	Individual adjustments	Net exposure	Gross exposure	Collective adjustments	Net exposure	Total (net exposure)
1. Financial assets available for sale							
2. Financial assets held to maturity				246,168		246,168	246,168
3. Due from banks				473,386		473,386	473,386
4. Due from customers	24,386	(17,416)	6,969	18,956	(503)	18,453	25,423
5. Financial assets carried at *fair value*							
6.Financial assets being disposed							
Total 2017	**24,386**	**(17,416)**	**6,969**	**738,510**	**(503)**	**738,007**	**744,977**
Total 2016	**24,842**	**(16,609)**	**8,233**	**1,223,726**	**(622)**	**1,223,104**	**1,231,337**

	Assets of evidently low credit		Other assets
	Cumulated capital losses	Net exposure	Net exposure
1. Financial assets held for trading			2,054,531
2. Hedging derivatives			
Total 2017			**2,054,531**
Total 2016			**1,831,693**

1.3 On- and off-balance sheet credit exposures to banks: gross and net values and past due brackets

Type of exposure/value	Gross exposure							
	Assets impaired							
	Up to 3 months	3-6 months	6-12 months	Over 1 year	Performing assets	Individual adjustments	Collective adjustments	Net exposure
A. On balance sheet exposures								
a) Bad loans								
- of which: forborne exposures								
b) Unlikely to pay								
- of which: forborne exposures								
c) Non-performing past due exposures								
- of which: forborne exposures								
d) Performing past due exposures								
- of which: forborne exposures								
e) Other performing exposures					991,108			991,108
- of which: forborne exposures								
Total A					**991,108**			**991,108**
B. Off-balance sheet exposure								
a) Non performing								
b) Performing								
Total B								
Total A + B					**991,108**			**991,108**

On-balance sheet exposures include all on-balance sheet financial assets claimed from banks, irrespective of their portfolio of allocation.

1.7 On- and off-balance sheet credit exposures to customers: gross and net values and aging

Type of exposure/value	Gross exposure							
	Non-performing assets							
	Up to 3 months	3-6 months	6-12 months	Over 1 year	Performing assets	Individual adjustments	Collective adjustments	Net exposure
A. On balance sheet exposures								
a) Bad loans				12,787		(12,787)		-
- of which: forborne exposures								
b) Unlikely to pay				11,599	-	(4,629)		6,969
- of which: forborne exposures								
c) Non-performing past due exposures								
- of which: forborne exposures								
d) Performing past due exposures								
- of which: forborne exposures								
e) Other performing exposures					1,801,932		(503)	1,801,430
- of which: forborne exposures								
Total A				**24,386**	**1,801,932**	**(17,416)**	**(503)**	**1,808,399**
B. Off balance sheet exposure								
a) Non performing								
b) Other					27			27
Total B					27			27
Total A + B				**24,386**	**1,801,959**	**(17,416)**	**(503)**	**1,808,426**

On-balance sheet exposures include all on-balance sheet financial assets claimed from customers, irrespective of their portfolio of allocation.

1.8 On-balance sheet credit exposures to customers: changes in gross non-performing exposures

	Bad loans	Unlikely to pay	Non-performing past due exposures
A. Initial gross exposures	9,876	12,098	2,868
- of which: exposures sold not derecognised			
B. Increases			
B.1 inflows from performing exposures	62		
B.2 transfers from other non-performing exposure categories	2,688		
B.3 other increases	342		
C. Decreases			
C.1 outflows toward performing exposures			
C.2 write-offs			
C.3 repayments	(181)	(499)	(180)
C.4 credit disposals			
C.5 losses from disposals			
C.6 transfers to other non-performing exposure categories			(2,688)
C.7 other decreases			
D. Final gross exposures	**12,787**	**11,599**	**-**
- of which: exposures sold not derecognised			

1.10 On-balance sheet non-performing credit exposures to customers: changes in total adjustments

Reason / Categories	Bad loans		Unlikely to pay		Non-performing past due exposures	
	Total	of which: forborne exposures	Total	of which: forborne exposures	Total	of which: forborne exposures
A. Initial total adjustments	**9,876**		**4,629**		**2,104**	
- of which: exposures sold not derecognised						
B. Increases						
B.1 impairment losses	725					
B.2 losses on disposal						
B.3 transfers from other non performing exposure categories	2,016					
B.4 other increases	342					
C. Decreases						
C.1 recoveries on impairment losses						
C.2 recoveries on repayments	(172)				(88)	
C.3 profits on disposal						
C.4 write-offs						
C.5 transfers to other non-performing exposure categories					(2,016)	
C.6 other decreases						
D. Final total adjustments	**12,787**		**4,629**		**-**	
- of which: exposures sold not derecognised						

2 Classification of exposures based on external and internal ratings

2.1 Detail off and on-balance sheet credit exposures by external rating class

Exposures	External rating classes							
	Class 1	Class 2	Class 3	Class 4	Class 5	Class 6	Unrated	Total
A. On balance sheet exposures	694,255	587,064	1,408,133	10,159	735		73,739	**2,774,085**
B. Derivatives								
B.1 Financial derivatives								
B.2 Credit derivatives								
C. Guarantees given							27	**27**
D. Commitments to lend funds								
E. Other								
Total	**694,255**	**587,064**	**1,408,133**	**10,159**	**735**		**73,766**	**2,774,112**

For the analysis of the credit risk of the borrowers / guarantors, the Institute uses S&P ratings; when S&P ratings are not available, the Institute utilizes the equivalent value from the Moody's rating agency.

In the preparation of the above table, S&P ratings have been used.

Below is a reconciliation between risk classes and the S&P ratings:

Class 1 – from AAA to AA-

Class 2 – from A+ to A-

Class 3 – from BBB+ to BBB-

Class 4 – from BB+ to BB-

Class 5 – from B+ to B-

Class 6 – Others

3 Detail of guaranteed credit exposures by type of guarantee

3.2 Guaranteed credit exposures to customers

		Real collateral (1)				Guarantees (2)									
						Credit derivatives					Credit commitments				
							Other derivatives								
	Net exposure	Real estate assets - mortgages	Real estate assets – financial lease	Securities	Other real guarantees	Credit Linked Notes	Governments and Central Banks	Other Public Entities	Banks	Other entities	Governments and Central Banks	Other Public Entities	Banks	Other entities	Total (1)+(2)
1. Guaranteed on balance sheet credit exposures															
1.1 totally guaranteed	435	435													435
- of which non performing															
1.2 Partly guaranteed															
- of which non performing															
2. Guaranteed off-balance sheet credit exposures															
2.1 Totally guaranteed															
- of which non performing															
2.2 Partly guaranteed															
- of which non performing															

5.2.4 Distribution and concentration of credit exposures

1. Detail by sector of on-balance and off-balance sheet credit exposures to customers (book value)

	Domestic			Foreign Public Sector												Foreign Private Sector											
	Public Authorities			Foreign Public Authorities			Regional – Local Public Authorities			International Public Authorities			Other Public Entities			Financial companies			Insurance companies			Non-financial companies			Other companies		
	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments
A. On-balance sheet exposures																											
A.1 Bad loans																										12,787	
- of which forborne exposures																											
A.2 Unlikely to pay																									6,969	4,629	
- of which forborne exposures																											
A.3 Non-performing past due exposures																											
- of which forborne exposures																											
A.4 Performing exposures	11,238			1,359,322												225,168			5,115			196,279			4,310		502
- of which forborne exposures																											
TOTAL A	**11,238**			**1,359,322**												**225,168**			**5,115**			**196,279**			**11,279**	**17,416**	**502**
B. Off-balance sheet exposures																											
B.1 Bad loans																											
B.2 Unlikely to pay																											
B.3 Other non-performing assets																											
B.4 Other exposures																									27		
TOTAL B																									**27**		
TOTAL (A+B) 2017	**11,238**			**1,359,322**												**225,168**			**5,115**			**196,279**			**11,306**	**17,416**	**502**
TOTAL (A+B) 2016	**8,290**			**1,354,046**												**237,021**			**9,286**			**239,360**			**17,590**	**16,609**	**622**

2. Detail by geographical area of on- and off-balance sheet credit exposures to customers (book value)

Exposures / Geographical areas	Domestic		European Countries		America		Asia		Rest of the world	
	Net exposure	Total adjust-ments	Net exposure	Total adjust-ments	Net exposure	Total adjust-ments	Net exposure	Total adjust-ments	Net exposure	Total adjust-ments
A. On-balance sheet exposures										
A.1 Bad loans				(12,787)						
A.2 Unlikely to pay			6,969	(4,629)						
A.3 Non-performing past due exposures										
A.4 Performing exposures	11,261	(3)	1,481,647	(485)	250,423		49,046	(13)	9,053	(1)
Total A	**11,261**	**(3)**	**1,488,616**	**(17,901)**	**250,423**		**49,046**	**(13)**	**9,053**	**(1)**
B. Off balance sheet exposures										
B.1 Bad loans										
B.2 Unlikely to pay										
B.3 Other non-performing assets										
A.4 Performing exposures			27							
Total B			**27**							
Total A+B 2017	**11,261**	**(3)**	**1,488,643**	**(17,901)**	**250,423**		**49,046**	**(13)**	**9,053**	**(1)**
Total A+B 2016	**8,326**	**(2)**	**1,601,032**	**(17,224)**	**217,127**		**50,415**		**5,923**	**(2)**

3. Detail by geographical area of on- and off-balance sheet credit exposures to banks (book value)

Exposures / Geographical areas	Domestic		European Countries		America		Asia		Rest of the world	
	Net exposure	Total adjust-ments	Net exposure	Total adjust-ments	Net exposure	Total adjust-ments	Net exposure	Total adjust-ments	Net exposure	Total adjust-ments
A. On-balance sheet exposures										
A.1 Bad loans										
A.2 Unlikely to pay										
A.3 Non-performing past due exposures										
A.4 Performing exposures	57,058		682,621		182,485		1,623		67,321	
Total A	**57,058**		**682,621**		**182,485**		**1,623**		**67,321**	
B. Off-balance sheet exposures										
B.1 Bad loans										
B.2 Unlikely to pay										
B.3 Other non-performing assets										
A.4 Performing exposures										
Total B										
Total A+B 2017	**57,058**		**682,621**		**182,485**		**1,623**		**67,321**	
Total A+B 2016			**976,812**		**148,537**		**1,396**		**70,736**	

4. Large exposures

IOR has no large exposures as defined by art. 46 of AIF Regulation No. 1.

5.2.5 Securitisation

No securitisation transactions were made by the IOR.

5.2.6 Information on unconsolidated structured entities

For unconsolidated structured entities, the Institute considers the shares held in externally managed investment funds.

For some external funds, the Institute is the owner of a significant number of shares, however, it does not control these funds because, it does not participate in investment decisions, either directly or indirectly, and it does not hold the ability to affect the returns of the above-mentioned funds.

The information required by IFRS 12 on the unconsolidated structured entities is below.

As of the balance sheet date, the Institute holds external funds in its trading portfolio for EUR 32.6m. Dividends collected in 2017 on such funds amount to EUR 400,000 (EUR 812,000 in 2016).

68% of the funds in the portfolio are closed-ended funds, and can be subscribed to only at given times by specific parties, who, as mentioned, have no control, and the remaining 32% of funds are related to funds that can be subscribed to by different entities at any time and for any amount (open-ended funds).

Conversely, with regard to their asset classes, funds held by the Institute invest in equity securities (27%), debt securities (32%) and the real estate market (41%). Regarding geographical distribution, the criteria used in the above mentioned table was used to separate funds based on their legally registered domicile.

According to those criterion, all of the funds are located within the European Union.

Investment Fund type	2017		2016	
	Balance sheet exposure		Balance sheet exposure	
	Nominal Value (quantity)	Carrying amount	Nominal Value (quantity)	Carrying amount
Open-end fund	75,160	10,326	75,160	10,404
Closed-end fund	19,770,677	13,322	20,170,677	13,333
Hedge fund				
Exchange traded fund				
Unit Investment Trust				
Fund of fund	2,300	8,932	2,300	9,944
Seed Fund				
Total	**19,848,137**	**32,580**	**20,248,137**	**33,681**
Underlying asset class focus				
Equity	2,300	8,932	2,300	9,944
Debt	75,160	10,326	75,160	10,404
Asset Allocation				
Money Market				
Real Estate	19,770,000	13,302	20,170,000	13,311
Commodity				
Alternative Investments	677	20	677	22
Total	**19,848,137**	**32,580**	**20,248,137**	**33,681**
Geographical Area				
UE	19,848,137	32,580	20,248,137	33,681
USA				
Total	**19,848,137**	**32,580**	**20,248,137**	**33,681**

At the balance sheet date, the IOR did not provide any guidance to unconsolidated structured entities on their investment policies. The Institute has not sponsored any unconsolidated structured entities.

At the balance sheet date, the Institute had a standing commitment to one of these funds to third parties of EUR 4m.

S.G.I.R. S.r.l. is 100% owned by IOR. The Institute does not prepare consolidated financial statements because the resulting information would not be relevant to the readers of the financial statements. The total balance sheet assets of the subsidiary are insignificant when compared with those of the Institute and, accordingly, the consolidated financial statements would not differ significantly from these financial statements.

5.2.7 Models for the measurement of credit risk

For the credit risk measurement, the Institute adopted the standard methodology defined by AIF Regulation No. 1, articles 63-89. No individual and portfolio internal models are used.

5.3 Market risks

Format and content of information on market risk and relative hedging policies

5.3.1 Interest rate risk and trading portfolio price risk

5.3.1.1 General aspects

Interest rate risk related to the trading portfolio is derived from the Institute's trading activity in financial instruments, both simple and complex, exchanged on organized markets and over-the-counter markets, put in place by the Treasury department. This risk pertains to positions in bonds, particularly those based on a fixed rate, the value of which is closely linked to the trend in interest rates. In line with the objectives of the Treasury Department in liquidity management and capital, and in line with the Institute's threshold for risk, the level of risk in the trading portfolio is rather low, as indicated by the short holding period (1.31 years). In anticipation of an increase in interest rates, the Institute has further reduced the overall holding period in order to mitigate any negative impact on the value of the portfolio.

Price risk comes from the exposure on equity securities, ETF and funds. The Institute reduced the threshold for such risk and exposures come mainly from the need to obtain a diversified return on own equity, in a period characterized by low interest rates.

5.3.1.2 Operating procedures and methods for measuring interest rate risk and price risk

Interest rate risk and price risk are measured and managed as part of the overall management and monitoring of risk.

Market risk is the risk of change in portfolio value from adverse fluctuations in market parameters, such as interest or currency rates, equity prices or prices of commodities underlying derivative contracts.

The Institute's trading portfolio is comprised mainly of bond securities, and the main associated risks are interest rate and LIBOR spread variation risk, as further described in the next paragraphs.

The power to assume market risk lies with the Directorate, which plays an active role in risk management and monitoring, according to the guidelines issued by the Board of Superintendence. Specifically, the Director General delegates the assumption of market risk and management to the Treasury department that operates autonomously in accordance with the limits assigned to the department.

Market risk assumption and management is separate from the confirmation, settlement, matching and execution (Back Office) and of the Risk Management department.

At 31 December 2017, the Institute did not hold quoted derivatives. A project analysing future interest rates is being performed, with the goal of providing an instrument for hedging the interest rate risk of the bond portfolio.

The system of measurement of financial risks and the establishment of operational limits of the Institute are based on the use of statistic calculation tools. Specifically, the three measures of potential loss are: Value at Risk, Expected Shortfall and Stress Test. These measures are defined as follows:

Value at Risk (VaR) is defined as the maximum loss that the Institute could withstand, with probability equal to predetermined confidence levels, in the case of adverse market trends to the position taken;

Expected Shortfall is defined as the average loss that the Institute could withstand in case of a VaR overrun;

Stress Test is defined as the loss that the Institute could withstand in case of negative events impacting main risk indicators (equity prices and indexes, interest rates, currency rates, credit spread) analyzed independently and as established by the RAF.

In addition to the aforementioned measures, the Institute utilises an indicator of realized losses on a 10-day time horizon, defined as the sum of the negative results realized on closed positions and unrealized losses on open positions, valued at market prices.

The VaR and the Expected Shortfall are calculated using the historic method (at least one year of data and quarterly update of the scenarios), with a daily timeline and confidence level at 99%.

The Stress Tests are calculated by simulating extreme scenarios of the main risk factors, starting from the worst movements recorded in the history of the world's financial markets, as further described in the following paragraphs. In particular:

- for interest rate risk, the variations in interest rates that make up the market curve, the rate volatility risk and correlation risk. On a daily basis, stress test analyses are conducted on the rates curve, assuming substantial shifts of the curve (-40% / +50% with a floor equal to 50 basis points);
- for LIBOR spread variation risk, the stress scenarios consider increases depending on the absolute spread level: more precisely, these are set equal to -20/+40 bps for securities with a spread lower than Libor, -40/+80 bps for securities with a spread between 0 and 100 bps and -40%/+80% of the spread for securities with a spread above 100 bps;
- for price risk, different categories of instruments are adequately presented: equities securities, equities indexes, funds and ETF. A stress test analysis is then conducted, applying the defined scenarios to spot prices (from -30% to +30%).

Monitoring compliance with limits on a daily basis is performed by the Risk Management department, which provides daily updates to the Directorate on the level of risk assumed and compliance with operational limits.

When operational limits have been exceeded, the Risk Management department promptly informs the Directorate of the overrun and the Director General decides on the appropriate action.

In establishing a system of market risk measurement, definition of operational limits, and the monitoring of compliance with the limits, the Director General is supported by the Risk Committee, who serves as an advisor on the following matters:

- assignment and review limits for of VaR, Expected Shortfall, Stress Test and WCL to the Treasury department;
- assignment of additional limits, determined based on nominal sensitivity factor (portfolio sensitivity to the single risk factors), etc;
- periodical trend analysis of the Institute's risk position and identification of the root causes of the unusual trends;
- monitoring risks assumed and compliance with the pre-established limits;
- total or partial disruption of the activities in certain sensitive financial instruments to risk factors;
- analysis of the ordinary and extraordinary events, following particular market turbulences and macroeconomic scenarios.

During 2017, the Institute maintained a prudential approach in the management of financial risks. Specifically, during the year, the held for trading portfolio had a daily average VaR of EUR 3.18m, a daily maximum VaR of EUR 3.55m and a daily minimum VaR of EUR 2.51m; the operational limits calculated on 10 working days, determined as EUR 25m under RAF, was never exceeded. At the end of 2017, the VaR amounted to EUR 7.5m. The portfolio only contained highly liquid products.

The Risk Management department, to verify the adequacy of the VaR calculation, periodically conducts retrospective reviews, comparing the actual trading results achieved, with the VaR measures previously calculated. During 2017, the Institute did not identify events where actual daily losses exceeded the risk measures expressed in terms of VaR on a daily basis.

The potential impact of a shock of +/- 100 basis point on the portfolio held for trading could have an impact of EUR 26.9m, representing 52.4%, 84.2% and 0.9% of interest margin, profit for the year and equity, respectively.

Stress test data at the end of 2017 shows, for interest rate risk, an exposure equal to EUR 14.0m for a variation of +50% of interest rates, with a minimum variation of 50 basis points; the exposure is focused on the EUR rate risk for 76% and on USD rate risk for the 23%.

The management and monitoring of risk is continuously improving. At the beginning of 2017, the implementation of the new system for the Treasury department has been completed; the system allows:

- monitoring of positions, profits and risks real time (automatic feed of main risk parameters and continuous revaluation of the position, calculation of the VaR position at any time of the day);

- possibility of monitoring P&L trend and risks in different aggregation levels, from the single instrument, to the entire position of the Treasury department.

2.1 Trading portfolio: detail by maturity date (re-pricing date) of financial assets and liabilities on balance sheet and financial derivatives

Type / Expiration date	On demand	Up to 3 months	3 - 6 moths	6-12 months	1 - 5 years	5-10 years	Over 10 years	Undefined
A. Cash assets								
1.1 Debt securities								
- with early redemption option				121,138	15			
- other	735,738	285,538	29,173	833,879	43,199	448		
1.2 Other assets								
2. Cash liabilities								
2.1 Repurchase agreements								
2.2 Other liabilities								
3. Financial derivatives								
3.1 With underlying security								
- Options								
+ Long positions								
+ Short positions								
- Other derivatives								
+ Long positions								
+ Short positions								
3.2 Without underlying security								
- Options								
+ Long positions								
+ Short positions								
- Other derivatives								
+ Long positions								
+ Short positions								

2.2 Trading portfolio: detail of equity securities and index exposures for the main countries quoted markets

Type / Quotation index	Quoted						
	Italian Stock Exchange	NYSE Arca	Xetra	New York	NASDAQ GS	Other	Not quoted
A. Equity securities							
- long positions	5,065	4,969	4,732	3,741	3,398	7,754	
- short positions							
B. Transactions not yet settled on equity securities							
- long positions							
- short positions							
C. Other derivatives on equity securities							
- long positions							
- short positions							
D. Derivatives on equity index							
- long positions							
- short positions							

The application of a 30% shock on the value of equity securities would have an impact of EUR 8.90 million, corresponding respectively to 17.3%, 27.9% and 0.3% of the intermediation margin, operating result and equity.

With reference to price risk of other financial instruments classified as held for trading, at the end of 2017, the Institute's portfolio had the following exposure:

- Closed-end funds EUR 22.3m;
- Open-end funds EUR 10.3m.

5.3.2 Interest rate risk and price risk of other financial instruments in portfolio

2.1 Other financial instruments in portfolio: detail by expiration date (re-pricing date) of financial assets and liabilities

Type / Expiration date	On demand	Up to 3 months	3 - 6 months	6 - 12 months	1 - 5 years	5 - 10 years	Over 10 years	Unde-fined
1. Cash assets								
1.1 Debt securities								
- with early redemption option					10,018			
- other		31,387	20,029	44,967	90,895	48,872		
1.2 Loans to banks	362,123	54,205		25,052	32,007			
1.3 Loans to customers								
- current accounts	11,254							
- other loans								
- with early redemption option	7,969							
- other	6,200							
2. Cash liabilities								
2.1 Due to customers								
- current accounts	2,121,948							
- other liabilities								
- with early redemption option								
- other		2,339	4,752	2,383				
2.2 Due to banks								
- current accounts	4,096							
- other liabilities								
2.3 Debt securities								
- with early redemption option								
- other								
2.4 Other liabilities								
- with early redemption option								
- other								
3. Financial derivatives								
3.1 With underlying security								
- Options								
+ Long positions								
+ Short positions								
- Other derivatives								
+ Long positions								
+ Short positions								
3.2 Without underlying security								
- Options								
+ Long positions								
+ Short positions								
- Other derivatives								
+ Long positions								
+ Short positions								
4. Other off balance sheet transactions								
+ Long positions								
+ Short positions								

Regarding interest rate risk for financial instruments other than those classified as trading, the Institute's exposure refers mainly to the assets classified as held to maturity and to interbank deposits, already listed in the paragraph related to credit risk.

The application of a variation of interest rates of +/- 100 basis points to the portfolio, including other financial instruments (EUR 246.17m) shows a potential impact of EUR 0.79m, in terms of variation of the coupon flow representing 2.7%, 2.5% and 0.03% of interest margin, profit for the year and equity, respectively.

The application of a variation of interest rates of +/- 100 basis points to the portfolio, including other financial instruments (EUR 246.17m) shows a potential impact of EUR 4.94m, in terms of changes in economic value representing 9.6%, 15.5% and 0.2% of interest margin, profit for the year and equity, respectively.

With reference to price risk of financial instruments not classified as trading, at the end of 2017, the Institute's portfolio had the following exposure:

- Financial assets available for sale EUR 4.6m;
- Investment in subsidiaries S.G.I.R. S.r.l. EUR 15.8m.

Regarding the limits, the Board of Superintendence established limits for the investment in financial assets held to maturity in relation to equity. For this portfolio, a measure of VaR is also calculated (respectively EUR 0.37m, 0.53m and 0.75m of minimum, medium and maximum daily value), but not associated with limits.

At the end of the year, the 10-day VaR was equal to EUR 1.22m.

5.3.3 Currency risk

General aspects, operating procedures and methods for measuring currency risk

Currency risk is the risk that the Institute can incur losses due to the adverse variation of currency rates. As mentioned above, the management of currency risk is based on the system in place for the management of financial risks.

For the currency rate, as it was for interest rates, the following pre-defined Stress Test scenarios were used for each currency providing shock higher for minor currencies and for those not related to Euro. The potential impact of these shocks could result in a loss of approximately EUR 1m.

2.1 Detail by currency of financial assets, liabilities and derivatives

Items	Currencies					
	USD	GBP	CAD	AUD	CHF	Other currencies
A. Financial assets						
A.1 Debt securities	475,658	5,000	192	2,418	3,427	173
A.2 Equity securities	9,949	1,220				6
A.3 Loans to banks	94,513	6,049	5,821	4,661	4,168	6,536
A.4 Loans to customers	107			-	23	-
A.5 Other financial assets	7,461	136	1,105	439	1,211	1,318
B. Other assets						
C. Financial liabilities						
C.1 Due to banks	304					
C.2 Due to customers	560,908	9,733	7,735	5,036	9,131	2,359
C.3 Debt securities						
C.4 Other financial liabilities	21,965	40	458	1,136	4	
D. Other liabilities						
E. Financial derivatives						
- Options						
+ Long positions						
+ Short positions						
- Other derivatives						
+ Long positions						
+ Short positions						
Total Assets	**587,688**	**12,405**	**7,118**	**7,518**	**8,829**	**8,033**
Total Liabilities	**583,177**	**9,773**	**8,193**	**6,172**	**9,135**	**2,359**
Difference (+/-)	**4,511**	**2,632**	**(1,075)**	**1,346**	**(306)**	**5,674**

The exchange rate risk exposure resulting from the application of the abovementioned stress tests of 100 basis points at 31 December 2017 resulted in an amount equal to EUR 0.07m, representing 0.1%, 0.2% and 0% of interest margin, profit for the year and equity, respectively.

2.2 Internal models and other methods for sensitivity analysis

For the capital requirement calculation related to currency risk, the IOR adopted the standard methodology provided by AIF Regulation No. 1.

5.3.4 Derivative instruments

In 2017 IOR did not hold derivative financial instruments.

5.4 Liquidity risk

Format and content of information on liquidity risk and relative hedging policies

5.4.1 General aspects, operating procedures and methods for measuring liquidity risk

Liquidity risk is the risk that the Institute will encounter difficulties in meeting payment obligations by cash or by expected or unexpected delivery, compromising the daily operations or the financial situation.

Regarding liquidity risk, during 2017, the IOR did not encounter any notable problems; at year-end 2017, the liquidity risk indicator (LCR), calculated over a period of 30 days, resulted in a value equal to 642%, well above the regulatory limit of 200% established by RAF. It is important to note that Institute liabilities are represented, other than equity, by deposits from customers, mainly on demand. Moreover, the Institute does not carry out funding transactions on the interbank market or on the capital market.

From an organizational standpoint, the Institute's liquidity risk is managed by the Treasury Department, which monitors the expected and realized flows in currencies and maintains an adequate portfolio of liquid assets to meet any unexpected payments.

Monitoring of liquidity and adherence to liquidity operating limits are performed daily by the Risk Management Department.

The following tables show the Institute's assets and liabilities with current values, divided by contractual maturities of the financial liabilities and the expected maturities of the financial assets. The first table includes only financial assets and liabilities in Euro, while the second table comprises only financial assets and liabilities in other currency than Euro.

1.1 Detail by contractual residual maturity of financial assets and liabilities in Euro

Type / Residual maturity	On demand	1 - 7 days	7 - 15 days	15 - 30 days	1 - 3 months	3 - 6 months	6 -12 months	1 - 5 years	Over 5 years	Undefined
Cash assets										
B.1 Government bonds			675	5,313	52,850	14,203	153,691	954,500	160,098	
B.2 Other debt securities	7	6	38,974	11,398	28,383	19,991	27,013	292,772	53,094	
B.3 UCI units										32,580
B.4 Loans										
- Banks	294,581						25,052	32,007		
- Customers	11,229	89			1	6	159	3,277	10,546	
Cash liabilities										
B.5 Deposits and current accounts										
- Banks	3,792									
- Customers	1,557,879									
B.6 Debt securities										
B.7 Other liabilities										
Off balance sheet transactions										
B.8 Financial derivatives with exchange of capital										
- long positions										
- short positions										
B.9 Financial derivatives without										
exchange of capital										
- long positions										
- short positions										
B.10 Deposits and loans to be settled										
- long positions										
- short positions										
B.11 Irrevocable commitments to										
lend funds										
- long positions										
- short positions										
B.12 Financial guarantees given										
B.13 Financial guarantees received										
B.14 Credit derivatives with exchange of capital										
- long positions										
- short positions										
B.15 Credit derivatives without exchange of capital										
- long positions										
- short positions										

1.2 Detail by contractual residual maturity of financial assets and liabilities in other currency than Euro

Type / Residual maturity	On demand	1 - 7 days	7 - 15 days	15 - 30 days	1 - 3 months	3 - 6 months	6 -12 months	1 - 5 years	Over 5 years	Undefined
Cash assets										
B.1 Government bonds	2,804		26	5	16,137	2,279	5,238	82,343	468	
B.2 Other debt securities		96	6,674	342	15,808	16,127	20,599	312,624	6,162	
B.3 UCI units										
B.4 Loans										
- Banks	67,542	54,205								
- Customers	25					91				
Cash liabilities										
B.5 Deposits and current accounts										
- Banks	304									
- Customers	564,068			167	2,172	4,752	2,383			
B.6 Debt securities										
B.7 Other liabilities										
Off balance sheet transactions										
B.8 Financial derivatives with exchange of capital										
- long positions										
- short positions										
B.9 Financial derivatives without exchange of capital										
- long positions										
- short positions										
B.10 Deposits and loans to be settled										
- long positions										
- short positions										
B.11 Irrevocable commitments to										
lend funds										
- long positions										
- short positions										
B.12 Financial guarantees given										
B.13 Financial guarantees received										
B.14 Credit derivatives with exchange of capital										
- long positions										
- short positions										
B.15 Credit derivatives without exchange of capital										
- long positions										
- short positions										

5.5 Operational risk

Format and content of information on operational risk and relative hedging policies

5.5.1 General aspects, operating procedures and methods for measuring operational risk

Operational risks represent the risk of loss caused by inadequate and failure of processes, human resources and internal system, or caused by external events.

Operational risk does not include strategic and reputational risks, but includes legal risk, which is the risk of loss from violations of laws and regulations, contractual or non-contractual liability, or other disputes.

Operational risks include, among other things, administrative risk (for example, absence or inadequacy of line controls), human resources risk (for example, a lack of professional training for staff), and IT risk (for example, inadequacy of the computer system that could cause loss of data or interruption of operations).

The Institute is defining a framework for operational risk management, establishing the organizational processes for measurement, management and control of that risk. More specifically, the risk assessment framework for the Institute's activities provides an assessment of the operational risk of each process (unmitigated risk), a verification of the tools for monitoring and mitigation of this risk and an assessment of the residual risks (mitigated risk).

Extraordinary losses and operating losses have been recorded during 2017 for a total amount of EUR 222,500 in consideration of the lower recovery compared to the returns expected by customers following unauthorized external transactions in 2016 related to external transactions not authorized (credit cards and payment services). However, it should be noted that the provision for allowances for risk and charges, allocated for EUR 3.5m as at 31 December 2016, was used for payment of previous tax issued with other countries for EUR 2.3m. The remainder, equal to EUR 1.2m, has been kept pending the formal conclusion on this issue.

For more information on contingent liabilities related to an investment fund held in a proprietary portfolio, refer to paragraph "Estimates that contain elements of uncertainty" in part 1.

PART 6. INFORMATION CONCERNING EQUITY

6.1 Shareholders' Equity

6.1.1 Qualitative information

The Institute's equity represents capital funding provided by the owner or generated by the business to create value.

In managing capital (a broader concept than "equity" presented in the balance sheet and consistent with regulatory capital, which is not comprised solely of equity in the strict sense), the Institute's objectives are:

- to safeguard the Institute's ability to continue as a going concern, so that it can continue to provide benefits for all stakeholders;
- to maintain a strong capital base to support business growth.

The Institute pursues its objectives of capital management during the planning processes, through the analysis of risks associated with planned activities, and during the monitoring processes through the analysis and monitoring compliance with limits.

In managing capital, the Institute observes regulatory capital requirements established by the regulatory framework related to prudential supervision.

6.1.2 Quantitative information

1 Detail

	2017	**2016**
1.Capital	300,000	300,000
2.Reserves		
a) Earning reserves		
(i) Unavailable	100,000	100,000
(ii) Available	282,134	282,134
(iii) Other		
b) Other		
3.Equity instruments		
4.Valuation reserves		
a) Available for sale assets	2,161	499
b) Tangible assets		
c) Intangible assets		
d) Hedging of foreign investments		
e) Cash flows hedging		
f) Exchange differences		
g) Non current assets held for sale		
h) Actuarial gains (losses) on defined benefit plans	(57,110)	(46,034)
i) Share of valuation reserves connected with investments carried at equity		
5.Profit (loss) for the year	31,934	36,001
Total	**659,119**	**672,600**

Capital, clearly identified as a component of Equity, represents a permanent endowment that cannot be reduced or distributed, except in case of cessation or liquidation of the entity.

Unavailable Reserves are profit reserves designed to further strengthen the Institute's Equity and long-term stability.

Available or "distributable" Reserves are earnings available for distribution, subject to a resolution of the Commission of Cardinals.

Fair Value Reserves for available for sale securities represent the net fair value gain/loss recognized on investment securities classified as available for sale.

Post-employment benefit actuarial gain (loss) Reserves represent the actuarial unrealised gain or loss related to the post-employment benefit plans.

2 Fair value reserve of financial assets available for sale: detail

	2017		2016	
	Positive Reserve	Negative Reserve	Positive Reserve	Negative Reserve
1.Debt securities				
2.Equity securities	2,161		499	
3.UCI units				
4.Loans				
Total	**2,161**		**499**	

3 Fair value reserve of financial assets available for sale: annual changes

	Debt securities	Equity securities	UCI units	Loans
1.Opening balance		**499**		
2.Positive changes				
2.1 Fair value increases		1,662		
2.2 Reclassification from negative reserves to the Income statement:				
From Impairment				
From disposal				
2.3 Other changes				
3.Negative changes				
3.1 Fair value decreases				
3.2 Impairment				
3.3 Reclassification from positive reserves to the Income statement:				
From disposal				
3.4 Other changes				
4.Closing balance		**2,161**		

4 Valuation reserves related to defined benefit plans: annual changes

	Defined benefit plan	Pension plan liabilities	Staff severance fund
1.Opening balance	**(46,034)**	**(44,292)**	**(1,742)**
2.Positive changes			
2.1 Post-employment benefit actuarial gain of the year	122		122
3.Negative changes			
3.1 Post-employment benefit actuarial loss of the year	(11,198)	(11,198)	
4.Closing balance	**(57,110)**	**(55,490)**	**(1,620)**

6.2 Own equity and prudential supervision ratios

1 Own equity

	2017	2016
A.Positive components		
1. Capital	300,000	300,000
2. Supplemental Capital		
a) Retained earnings		
(i) Unavailable	100,000	100,000
(ii) Available	282,134	282,134
(iii) Others		
b) Provisions		
c) Reserves	(54,948)	(45,535)
3. Positive prudential filter IAS/IFRS		
B.Negative components		
1. Goodwill		
2. Intangible assets	(871)	(1,044)
3. Impairments on loans		
4. Losses recognized in previous years and in current year		
5. Regulatory downs of assets carried at fair value		
6.Negative prudential filter IAS/IFRS	(1,081)	(250)
Common Equity	**625,234**	**635,305**

Capital is defined by AIF Regulation No.1 art. 3 (8) as the initial funding or subsequent integration of capital by the Holy See or the Vatican City State.

a) it is paid pursuant to the legislation of the Holy See and the Vatican City State;

b) it is clearly and distinctly identified in the financial statements;

c) it cannot be reduced or distributed, except in the case of cessation or liquidation of the entity, ensuring that it is distributed proportionality to legitimate creditors, according to the legislation of the Holy See and the Vatican City State and acquired by the Apostolic See.

For regulatory purposes, the term "Capital" shall be considered as equivalent to "core capital".

The Supplemental Capital is defined under AIF Regulation No. 1 art. 3 (68) as the sum of retained earnings, accumulated as other comprehensive income and other reserves.

The Common Equity is defined under Regulation No. 1, art. 3 (12) as:

- the sum of the following positive components:
  - a. the Capital;
  - b. the supplemental capital;

- deducting the following components (if negative):
  a. goodwill;
  b. intangible assets;
  c. adjustments to the value of receivables;
  d. losses recognized in previous financial periods and in the current period;
  e. adjustments to the regulatory value of assets valued at their "fair value".

For regulatory purposes, "common equity" shall be considered as equivalent to "common equity tier 1".

Regulatory capital consists of common equity and is calculated by the Institute on a monthly basis, although only required to be calculated by the Supervisory Authority quarterly.

As required, the amount of annual and half-yearly earnings, excluding the amounts that can potentially be allocated to dividends, contributes to the calculation of regulatory capital for the months of December and June.

The Common Equity at the end of 2017 amounted to EUR 625.2m (2016: EUR 635.3m).

Considering the items comprising the Institute's equity, the sole prudential filter in common equity at 31 December 2017 is associated with the positive fair value reserve relating to the investment securities held in the Available for Sale portfolio. This reserve is computed using a negative prudential filter, for an amount equal to 50%.

In the calculation of the Regulatory Capital 2017, the Net profit for the year not included, as it is considered fully distributed.

6.2.2 Capital adequacy

The monitoring of key ratios is performed daily by the Risk Management Department, in order to continuously monitor compliance with regulatory requirements. The table below shows the data relating to capital requirements at the end of 2017 and at the end of 2016 for comparison.

	Unweighted amounts		Weighted amounts/ Capital requirements	
	2017	2016	2017	2016
A. Risk asset				
A.1 Credit and counterparty risk				
1. Standardised approach	861,541	1.333,514	306,678	360,173
2. Approach based on internal ratings				
2.1 Based				
2.2 Advanced				
3. Securitizations				
B. Capital requirements				
B.1 Credit and counterparty risk			24,534	28,814
B.2 Credit valuation adjustment risk				
B.3 Settlement risk				
B.4 Market risk				
1. Standardised approach			41,700	40,245
2. Internal model				
3. Concentration risk				
B.5 Operational risk				
1. Basic indicator approach			7,043	9,699
2. Standardised approach				
3. Advanced approach				
B.6 Other calculation elements				
B.7 Total capital requirements			73,278	78,758
C. Risk weighted assets and capital ratios				
C.1 Risk-weighted assets			915,971	984,472
C.2 Capital/ Risk-weighted assets			32.75%	30.47%
C.3 Common equity/Risk-weighted assets			68.26%	64.53%

PART 7. RELATED PARTY TRANSACTIONS

Related parties of the Institute include key management personnel (Directorate and Board of Superintendence), the Commission of Cardinals and the *Revisori*.

Transactions with these related parties relate to salaries and remuneration

Details of key management compensation

Compensation due to related parties was EUR 731,200 in 2017, of which EUR 323,200 was not yet paid as of 31 December 2017. Specifically, these expenses relate to:

- EUR 340,000 for the Board of Superintendence of which EUR 240,000 has not yet been paid;
- EUR 308,000 for the Directorate;
- EUR 83,200 for the *Revisori*, completely to be paid.

These amounts are recognized in the Income Statement as Operating Expenses.

Related-party transactions

During 2017, no transactions with key management were entered into, except for the management of the deposit accounts opened with the Institute and salaries and remuneration discussed above.

As of the balance sheet date, the balance of deposits by the members of the Commission of Cardinals was EUR 3.02m.

Key management personnel and *Revisori* had deposits totaling EUR 33,000.

The Institute has a long-term zero-interest loan to its subsidiary S.G.I.R. S.r.l., amounting to EUR 2.8m. Furthermore the Institute signed the loan for the use of 5 real estate properties at no cost with its subsidiary, S.G.I.R. S.r.l. During 2017, S.G.I.R. S.r.l. earned rental income for EUR 57,000 on these properties.

IOR

Istituto per
le Opere
di Religione

Report of the Revisori

To the Board of Superintendence of the Istitute

In this report, drawn up in accordance with Article 28 of the Statute, the Board of Auditors of the Institute (the "Institute" or the "IOR") remarks on the annual financial statements, the report and the supporting documents, as prepared by the Directorate for the financial year 2017.

As in previous years, once again in the course of this year in performing its tasks the Board of Auditors has been constantly focused on proving its full loyalty and compliance with the Will of the Holy Father, who demands respect for the Statutory provisions and impartiality and independence in our role.

During the financial year, the Board of Statutory Auditors convened periodically to perform its duties and attended, upon invitation, all the meetings of the Board of Superintendence.

The meetings of the Board of Auditors were characterized by intense work sessions and benefited from the members' diverse skills as well as the solid support of the President, the Directorate and, where necessary, the Institute's Administration and Control Functions.

The Board also noted that in 2017, through the provision of dedicated services, the Institute confirmed its commitment to serving the Holy Father in the fulfilment of his mission as universal pastor.

Activities carried out in compliance with the Statute's provisions

The Board reports that, in accordance with Article 27 of the Statute, during 2017 it carried out the audits of treasury assets falling within its jurisdiction, as well as the administrative and accounting review of the books and accounts, also by obtaining information from the heads of the internal control functions, and has no remarks to make in this respect.

2017 financial statements

Pursuant to Article 28 of the current Statute, the Board of Auditors of the Institute examined the 2017 financial statements ("Financial Statements") and the Management Report.

The Financial Statements were drawn up in accordance with the Circular on the Preparation of the Annual Financial Statements and Consolidated Financial Statements of Entities carrying out Financial Activities on a Professional Basis, issued by the Financial Information Authority on 15 December 2016; the comparison with the previous year's data is consistent given that the financial statements at 31.12.2016 had already been drawn up in accordance with the provisions laid down in the previously mentioned Circular Letter

The Financial Statements are made up of the following:

- Balance Sheet
- Profit and Loss Statement
- Comprehensive Profit and Loss Statement
- Statement of Changes in Equity
- Statement of Cash Flows

The Annual Report includes the above documents as well as a description of the Institute's activities, a summary of the accounting policies as well as the risks and uncertainties linked to the use of estimates, the explanatory notes to the Financial Statements, and financial risk information prepared in accordance with the Vatican rules on prudential supervision.

The Financial Statements may be summarised as follows:

	EUR000
BALANCE SHEET	
Total assets	2,999,008
Total liabilities	2,339,889
Net assets	659,119
PROFIT AND LOSS ACCOUNT	
Net result from financial activities	50,933
Net operating profit	31,934

The Financial Statements have been audited by Deloitte & Touche S.p.A., which expressed a clean and unqualified opinion on 20 April 2018.

Based on the audits that have been performed, and taking into account the conclusions drawn by the internal control functions and the audit firm's unqualified opinion, this Board of Auditors:

- is in favour of the approval of the 2017 financial statements (Financial Statements) included in the Annual Report, as prepared by the Directorate;
- agrees with the proposed allocation of the net operating profit.

The approval of the 2017 Annual Balance Sheet (Financial Statements) has also coincided with the end of the current Board of Auditors' mandate. We wish to thank the Commission of Cardinals and the Board of Superintendence for the confidence they have placed in us and also the Institute's governing bodies for their constant and effective cooperation that has enabled us to provide our professional assistance, serving the Holy Church and the Holy Father.

Vatican City State, 20 April 2018

President of the Board of Statutory Auditors

This report has been translated into the English language solely for convenience of international readers.

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Istituto per le Opere di Religione

Report of the External Auditors

Deloitte.

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INDEPENDENT AUDITOR'S REPORT

To the Members of the Superintendence Board of Istituto per le Opere di Religione

Opinion

We have audited the financial statements of Istituto per le Opere di Religione (the "Institute"), which comprise the balance sheet as at December 31, 2017 and the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended and explanatory notes including a summary of significant accounting policies.

In our opinion, the financial statements give a true and fair view of the financial position of the Institute as at December 31, 2017, of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and the requirements of the regulations issued by the Financial Intelligence Authority of the Vatican City State (the "Requirements").

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Institute in accordance with the ethical and independence principles of the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants and we have fulfilled our responsibilities in accordance with these principles. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Information

The Board of Superintendence and the Directorate are responsible for the preparation of the sections of the management report within their respective competence in accordance with the Requirements.
Our opinion on the financial statements does not cover the management report and we do not express any form of assurance conclusion thereon.

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

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Responsibilities of Directorate for the Financial Statements

The Directorate is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards adopted by European Union as well as the Requirements and for such internal control as it 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 Directorate is responsible for assessing the Institute'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 Directorate either intends to liquidate the Institute 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 ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Institute's internal control;
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by Directorate;
- conclude on the appropriateness of Directorate's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Institute'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 Institute to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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We communicate with those charged with governance regarding, identified at an appropriate level as required by ISAs, 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.

DELOITTE & TOUCHE S.p.A.

Signed by
Antonio Sportillo
Partner

Rome, Italy
April 20, 2018

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Rome, 22 May 2018