2. Securities and off-balance sheet transactions
(excluding foreign currency transactions)

The security portfolio is divided into "Investment portfolio" and "Trading portfolio".

Securities registered in the investment portfolio reflect precise predefined strategic decisions taken by Company management. Such securities may be sold before maturity provided a change in management strategy occurs, or if market conditions evolve so to undermine reasons which had brought about the inclusion of such securities in the investment portfolio.

Both securities held for trading and those purchased for liquidity purposes are recorded in the trading portfolio.

Book value of zero-coupon securities has been accounted plus the value of accrued interest matured.

2.1 Investment portfolio

Securities classified as financial fixed assets are recorded and valued at purchase cost or, if transferred from the trading portfolio, at their book value at the time of transfer.

Investment securities are only written down if a permanent loss of value has occurred in relation to the solvency of the issuer and of the borrowers' resident Countries. Their original value is reinstated in subsequent years, to the extent that the reasons for any write-downs cease to apply.

Issue discounts in relation to these securities are registered among interest income on an accruals basis, as an increase in their book value. The difference between purchase cost, including accrued issue discounts, and the higher or lower principal repayment of investment securities goes to increase or decrease interest income which is recognised on an accruals basis.

2.2 Trading portfolio

This comprises securities recorded on a LIFO basis using annual layers.
Issue discounts in relation to debt securities are recognised on an accruals basis among interest income as an increase in their book value.

The valuation is carried out as follows:

- Italian and foreign securities traded on regulated markets:
  average market price for the last month of the year;
- unlisted securities:
  at the lower between cost or market value; the latter is calculated considering estimated realisable value which, in the case of fixed-income securities, is determined by discounting future financial flows using the market interest rate, obtained on listed securities with similar characteristics or on information system based markets normally used internationally. The solvency of the issuer and the resident Country difficulty in servicing debt is also considered.

Value of written down unlisted securities is reinstated in subsequent years, to the extent that the reasons for any write-downs cease to apply.

Repurchase agreements are treated as deposit-taking or lending transactions.

In particular:

- spot sales with a commitment to repurchase are recorded as deposits and stated at the spot amount received;
- spot purchases with a commitment to resell are recorded as loans and stated at the spot amount advanced.

In repurchase agreements on fixed-income securities, the difference between the spot and forward tel quel prices represents interest expense on deposits and interest income from loans and is recognised on an accruals basis.
Transactions in securities and similar instruments are recorded with reference to their settlement dates.

2.3 Off-balance sheet transactions (excluding foreign currency transactions)

Dealing securities to be delivered or received in relation to completed contracts that have not been settled at balance-sheet date are considered as a part of the trading portfolio and are valued as described above, considering the forward price contained in the contract. Any write-downs are offset by corresponding adjustment in the "Other liabilities" section of the balance sheet.

Off-balance sheet transactions which refer to derivative contracts on securities, on interest rates, or on indices are valued as follows:

- derivatives used to hedge assets and liabilities (both on- and off-balance sheet) have been valued on a consistent basis with assets and liabilities hedged;
- derivative contracts held for trading are stated at market value;
- derivative contracts which are part of "complex financial portfolios" (made up of various derivative contracts, securities held for trading, forward purchases to be settled) and managed as a single contract in order to achieve a specific result, are stated at market value.

Market value for derivative contracts has been calculated on the basis of the official end-of-year quotation for derivatives traded in regulated markets and according to estimated substitution costs for derivatives which, though unlisted, can be considered similar to listed derivatives since they use as parameters prices, quotations or indices that may be obtained from international information systems and can, in any case, be calculated objectively.

Differentials on hedges on interest-bearing assets or liabilities are recognised on the basis used to record the interest itself, in the case of specific hedges, or over the life of the contract (in the case of general hedges).

Differentials on hedges on non-interest-bearing assets or liabilities are recorded in the statement of income at the time of settlement.

Differentials on multi-flow derivative contracts held for trading are registered in the statement of income over the life of the contracts. Differentials on single-flow derivatives are registered at the time of settlement.

Results of off-balance sheet transactions are accounted for in the balance sheet without offsetting assets and liabilities.

3. Equity investments

Significant investments are consolidated, as described in the consolidation criteria.

Other minority equity investments are recorded on a LIFO basis using annual layers and stated at cost as they are financial fixed assets.

In this regard, the book value of investments held as at 31st December 1992 (which includes any revaluations carried out according to specific regulations) is deemed to represent their cost at that date, as permitted by Art. 8.4, of Legislative Decree 87/92.

As allowed by current fiscal legislation, the book value of equity investments may be written down, in the case of securities listed in regulated markets, also considering market values, estimated using the average prices in the six-month period.

Book value is written down to reflect any permanent reductions in the value of equity investments. However, the original value may be reinstated in subsequent years, to the extent that the reasons for any write-downs cease to apply.

Dividends and related tax credits are recorded in the year they are declared, which corresponds to the time of collection.

4. Assets and liabilities in foreign currency
(including off-balance sheet transactions)

Other assets and liabilities denominated in foreign currencies are translated into lire using end-of-year spot exchange rates with the sole exception of equity investments.

Off-balance sheet transactions in foreign currencies including derivative contracts are stated as follows:

- for transactions related to spot contracts to be settled, the values have been calculated using spot exchange rates at the end of the year;
- for transactions related to forward contracts, the values have been obtained using end-of-year forward rates for maturities corresponding to those on the relative contracts;
- for transactions related to specific assets or liabilities, the values have been calculated on a consistent basis and take into account the terms and conditions contained in the relative contracts.

Assets, liabilities and off-balance sheet transactions denominated in currencies which are part of the euro, or are in any case linked to the value of currencies which are part of the euro, have been translated into lire by applying the respective conversion exchange rates, with the exception of equity investments for which the spot exchange rate at the date of purchase has been used as specifically provided for in Art. 21 of Legislative Decree 213/98.

Differentials between the spot and forward rates applying to hedging transactions are recognised in the statement of income on an accruals basis, to match the recognition of interest on the underlying assets or liabilities.

Foreign currency transactions are recorded with reference to the time of settlement.

5. Tangible fixed assets

Real estate is recorded at purchase cost, including related charges, as well as renovation expenses and any extraordinary repairs, which have determined an increase in its value.

The value of certain real estate properties has also been restated as a result of applying revaluation laws and following the allocation of merger deficit or, in the consolidated financial statements, as a result of positive consolidation differences.

Furniture, furnishings, installations and machines are recorded at purchase cost, including related expenses and any improvement expenditure incurred.

The book value of tangible fixed assets is stated net of accumulated depreciation. These assets are automatically depreciated on a straight-line basis using rates which reflect their useful lives.

In particular:

- newly-acquired assets are depreciated from the accounting year in which they enter service;
- assets entering service during the year are depreciated at half the standard rate since it is assumed that, on average, their use began half way through the year. This approach is also acceptable for fiscal purposes.

Tangible fixed assets identified on the consolidation of inter-company leasing transactions are depreciated on the above basis; the depreciation rates applied by the user are adopted for this purpose.

Advance depreciation provided for fiscal purposes is reversed on consolidation and provision is made for the related deferred taxation.

Maintenance expenditure that does not increase the value of assets is expensed as incurred.

6. Intangible fixed assets

Intangible fixed assets are stated at purchase cost net of accumulated amortisation.

This caption comprises:

- goodwill paid on the acquisition of companies and negative merger balances which emerge on integration of companies. These are amortised at constant rates over a ten-year period. Positive consolidation differences are considered intangible fixed assets even though these are accounted for in specific captions in the consolidated financial statements; these are amortised at constant rates over a ten-year period just like goodwill;
- start-up costs related to new branches located in buildings which are not owned by the Group, costs related to new issues of shares or of other securities. Such costs are amortised at constant rates over a five-year period;
- refurbishing costs for branches and other premises which are not owned by the Group. These costs are amortised on a straight-line basis over the shorter period between their estimated useful life and, in any case, according to provisions set out by Art. 16.1 of Legislative Decree 87 of 27th January 1992, not over five years;
- application software costs of multi-annual use. These are amortised over a maximum of five years according to estimated useful life;
- other deferred charges which are amortised over a maximum period of five years. Value of intangible fixed assets is adjusted when losses deemed to be permanent occur.

7. Other policies

7.1 Accruals and deferrals

Accruals and deferrals are determined in accordance with the matching principle, taking account of the rates and conditions applicable to individual accounts.

The amounts are reported separately in the balance sheet since, as permitted, they have not been added to or deducted from the asset and liability accounts to which they relate.

The only exceptions to this refer to accruals on zero-coupon securities (certificates of deposit and bonds) in the securities portfolio and zero-coupon securities (certificates of deposit and bonds) issued by Group companies.

7.2 Deposits and public funds under administration

Deposits of banks and ordinary customers and public funds under administration are stated at their nominal values.

7.3 Securities in issue

Mortgage bonds, other bonds, certificates of deposit and bank cashiers' cheques are stated at their nominal values. Zero-coupon securities (certificates of deposit and bonds) have been stated at issuance price plus the accrued interest matured during the year.

Residual portion of any discounts on bonds issued below par is reported as a prepaid expense. Residual premium on bonds issued above par is recorded as a deferred income item.

7.4 Allowance for employee termination indemnities

The amount recorded represents the liability to all employees at the end of the year, accrued in accordance with current legislation and labour agreements.

7.5 Allowances for risks and charges

- Allowance for post retirement benefits and other similar obligations
  It has been constituted as a consequence of specific contracts and is sufficient to guarantee the payment of pensions for which the Group is liable.
- Taxation
  The provision for income taxes is determined with reference to a prudent estimate of the current tax charge, prepaid taxation and deferred taxation of realised capital gains.

  In particular, prepaid and deferred taxes are determined according to all the temporary differences between the value attributed to an asset or a liability based on the Italian Civil Code accounting principles and the correspondent values for fiscal purposes (irrespective of temporal limits). Asset captions related to prepaid taxes are accounted for in the balance sheet when a reasonable certainty of their recovery exists, based on the company's continuing capacity to generate taxable income.

  Liabilities related to deferred taxes, as already occurred in previous years, have been fully accounted for, with the sole exception of shareholders' equity reserves for which taxes are suspended, since it is reasonable to believe that no voluntary actions will be taken for the purpose of taxing such reserves.

  Prepaid and deferred taxes are accounted for in the balance sheet with open balances and without offsetting effects, the former in the "Other assets" caption and the latter in the "Allowances for risks and charges – allowance for taxation" caption.

  In addition, this account reflects the deferred taxation on consolidation adjustments, if it is likely that the taxes concerned will become payable by a Group company. These taxes essentially reflect:
  - those arising from the elimination on consolidation of adjustments and provisions recorded solely for fiscal purposes;
  - those arising from the registration of positive consolidation differences in the assets of the consolidated company.

  Assets and liabilities related to prepaid or deferred taxes are systematically valued considering any changes in fiscal regulations or tax rates and the situation of the company involved.

  The allowance also contains provisions for tax charges which could derive from controls already notified, or in any case from litigations currently under way with the tax authorities.

- Other allowances
  This caption comprises provisions made to cover known or likely losses, the timing or the extent of which cannot be determined at the balance sheet date.
  Such allowances do not adjust the value of corresponding assets.
  The allowances reflect the best estimate of the charges to be incurred, based on available information.

7.6 Allowance for possible loan losses

The allowance for possible loan losses has been set up for prudential purposes, considering loan portfolio composition. The item contains provisions for capital losses and provisions for interest on non-performing loans.

7.7 Subordinated liabilities

These are stated at nominal value.

Foreign currency subordinated liabilities are translated using the end-of-year spot rates.