INFRA BANKING EXPERTS
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KOMMUNAL
KREDIT

ANNUAL REPORT OF KOMMUNALKREDIT GROUP

2017

BUILDING BRIDGES

WE PROVIDE TANGIBLE BENEFIT
TO THE COMMUNITY

WE PROVIDE TANGIBLE BENEFIT TO THE COMMUNITY

Significant growth in new business

26 projects with commitments worth EUR 635m

Well-balanced new business portfolio

Strongly diversified in terms of product, region and asset class

Funding position enhanced

Customer deposits more than tripled to EUR 644m

Robust result

IFRS profit after tax EUR 18.1m

High quality of loan portfolio

Average rating »A«
NPL ratio 0.0%

Solid capital position

CET 1 ratio 23.5%
Total capital ratio 29.9%

Launch of online retail platform

KOMMUNALKREDIT INVEST with deposits of EUR 116m in first three months

HIGHLIGHTS 2017

Kommunalkredit is well on track as a strong player in the European infrastructure market.

- **Origination – significant growth in new business:** Kommunalkredit managed to close 26 projects in 13 countries with commitments worth EUR 635.2m delivering a P&L impact significantly above plan.
- **Distribution:** Kommunalkredit placed EUR 373.2m of its portfolio with institutional investors and banks. Thereof EUR 194.2m stemmed from new business origination across 9 projects. The successful distribution activity testifies to new business transactions' market conformity in terms of structure, pricing and risk management.
- **Strong client impact:** Kommunalkredit expanded its network of anchor clients evidenced by transaction award from repeat client relationships and a widely diversified group of institutional investors, such as insurance companies, pension funds, banks, family offices and infrastructure funds.
- **First industry awards:**
  - Kommunalkredit was awarded its first industry accolades from leading infrastructure journals, which included the "Europe Transport Deal of the Year" by *PFI* and a "Top 10 Infrastructure Deal" by *Inspiratia*.
  - In a ranking by the Austrian finance magazine *Börsianer*, Kommunalkredit was chosen as the country's top "Specialist Bank" and as the third best bank in Austria, based on strategic innovation.
- **Well-balanced portfolio mix of new business:** In 2017 new business was strongly diversified in terms of product, region and asset class with attractive risk/return profiles and a decreasing duration, thus contributing to an improved asset-liability match.
- **High quality of the loan portfolio:** As of 31 December 2017, the average rating of the loan portfolio was "A", with 89.4% of the loans being investment grade. The non-performing-loan (NPL) ratio was maintained at 0.0% in 2017. The weighted average probability of default was 0.23%.
- **Team and processes strengthened:** The front office team was strengthened by hiring highly experienced experts with a strong international track record, whilst in parallel Kommunalkredit enacted a cost efficiency programme which will lead to a reduction of the cost base in 2018.
- **Funding position enhanced:** Kommunalkredit more than tripled its customer deposits to EUR 644.4m driven by both wholesale and retail deposits. As a major strategic initiative, the bank launched its new online retail platform KOMMUNALKREDIT INVEST in 2017. In addition, Kommunalkredit successfully returned to the capital market with a "Debt Issuance Programme", under which it issued a social covered bond and, for the first time since its privatisation in 2015, a senior unsecured bond.
- **Solid capital position:** As of 31 December 2017, Kommunalkredit's total capital ratio amounted to 29.9%. Its CET 1 ratio stood at 23.5%.
- **Rating:** Kommunalkredit's unsecured debt issues remained stable at investment grade level with a long-term rating of "BBB (low)" (negative trend) and a short-term rating of "R-2 (mid)" from the DBRS rating agency. Standard & Poor's rated Kommunalkredit's covered bonds for the first time on 13 June 2017, assigning them an "A" rating.

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BOARDS
OF THE BANK

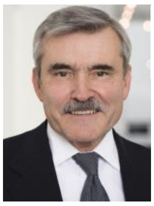
EXECUTIVE BOARD

Alois Steinbichler
Chief Executive Officer

Jörn Engelmann
Member of the Executive Board

Karl-Bernd Fislage
Member of the Executive Board
since 1 February 2017

Wolfgang Meister
Member of the Executive Board



Alois
Steinbichler

Jörn
Engelmann

Karl-Bernd
Fislage

Wolfgang
Meister

SUPERVISORY BOARD

Patrick Bettscheider
Chairman; delegated by Interritus Limited

Christopher Guth
Deputy Chairman; delegated by Attestor Capital

Friedrich Andreae
Delegated by Attestor Capital; Managing Director Gesona Beteiligungsverwaltung GmbH and Satere Beteiligungsverwaltungs GmbH

Katharina Gehra
Delegated by Interritus Limited; Managing Director Gesona Beteiligungsverwaltung GmbH and Satere Beteiligungsverwaltungs GmbH

Jürgen Meisch
Managing Director Achalm Capital GmbH

Werner Muhm
Former Director of the Vienna Chamber of Labour and the Federal Chamber of Labour
until 10 March 2017

Martin Rey
Managing Director Maroban GmbH
since 24 July 2017

Patrick Höller
Delegated by the Staff Council

Franz Hofer
Delegated by the Staff Council
until 6 November 2017

Paul Matousek
Delegated by the Staff Council
since 6 November 2017

Renate Schneider
Delegated by the Staff Council
since 20 February 2017

STATE COMMISSIONER

Edeltraud Lachmayer
State Commissioner; Federal Ministry of Finance

Bettina Horvath
Deputy State Commissioner; Federal Ministry of Finance

GOVERNMENT COMMISSIONER FOR THE COVER POOL FOR COVERED BANK BONDS

Karin Fischer
Government Commissioner; Federal Ministry of Finance

Sandra Kaiser
Deputy Government Commissioner; Federal Ministry of Finance

FOREWORD
BY THE CHIEF EXECUTIVE OFFICER

Ladies and Gentlemen,

I am pleased to present the Annual Report of Kommunalkredit Austria AG (Kommunalkredit) for the financial year 2017. The bank is well on track to meet its growth targets. We achieved or exceeded our main objectives for 2017 and our success is being increasingly recognised in the European infrastructure market. Kommunalkredit bridges the needs of project sponsors (developers and operators of infrastructure) and institutional investors, such as insurance companies, pension funds or banks, for whom infrastructure has become an increasingly attractive asset class.

In 2017, Kommunalkredit Group generated a consolidated IFRS after-tax result of EUR 18.1m (2016: EUR 49.0m). The decrease compared to the previous year resulted from the expected decline in one-off positive effects relating to the buyback of own issues in 2016. The result for 2017 reflects the increasing new business volume, which made a growing contribution to both net interest income and fee and commission income.

Last year, we completed 26 projects with commitments worth EUR 635m across 13 European countries. We played a leading role in notable projects, acting as Mandated Lead Arranger or Co-Arranger, and we were awarded our first industry accolades. In addition to the origination of new business, the placement of financing with end investors is one of the bank's strategic objectives. The bank showed a strong performance by placing a volume of EUR 373m with a variety of leading institutional investors.

We implemented major strategic initiatives. The launch of our online retail platform KOMMUNALKREDIT INVEST represents Kommunalkredit's first product offering for retail customers. Following the appointment of Bernd Fislage as Member of the Executive Board, assuming responsibility for Banking & Markets, our front office team was strengthened with the recruitment of experienced senior bankers. In parallel, we enacted an efficiency programme to streamline internal processes, which will lead to a reduction of the cost base in 2018. The bank's funding position was enhanced significantly. We managed to triple customer deposits to EUR 645m. Furthermore, the bank returned to the capital market with the emission of a EUR 300m social covered bond, the first of its kind in Austria.

Kommunalkredit enjoys a very solid capital position. It reports a total capital ratio of 29.9% and a CET 1 ratio of 23.5%. The bank holds a loan portfolio of high asset quality without a single default in 2017. The average rating of the portfolio was "A", with 89.4% of the loans being investment grade. The non-performing-loan (NPL) ratio was maintained at 0.0%.

Based on the progress achieved in the business year 2017, Kommunalkredit is well-positioned to benefit from the opportunities in the European infrastructure market. A dynamic project pipeline promises a continuation of a successful year. With a rising operating result and a continued decline in extraordinary income, Kommunalkredit expects its annual result for 2018 to be above the previous year's level.

We have started 2018 with a dynamic project pipeline. On behalf of the Executive Board, I would like to take this opportunity to thank our clients and business partners most cordially for their excellent cooperation and the trust placed in us. Our thanks also go to our shareholders for their active support and to our employees for their great commitment, which they once again showed over the previous year.

Yours sincerely,

Alois Steinbichler
Chief Executive Officer of Kommunalkredit Austria AG

MANAGEMENT REPORT FOR THE BUSINESS YEAR 2017

ECONOMIC FRAMEWORK

Economic environment in 2017

In 2017, the economy of the euro zone experienced the strongest growth since 2007, picking up by 2.4% compared to 1.8% in 2016. Gross domestic product (GDP) rose by 2.2% in Germany (2016: 1.9%) and by 1.8% in France (2016: 1.2%). The pace of economic growth in Austria was exceptionally fast at 3.1% (2016: 1.5%), whereas the British economy was notably depressed in the context of the looming Brexit, with GDP climbing by only 1.8% (2016: 1.9%).[1]

Especially in the euro zone, the economic growth momentum observed in 2017 was robust and broad-based, driven primarily by private consumption and business investment. Furthermore, growth was supported by steadily rising private income and corporate profits as well as expanded lending spurred by favorable financing conditions. Growth was more balanced and self-sustained across countries and sectors. Household consumption in particular was backed by a solid increase in disposable income and consumer confidence.

The unemployment rate in the euro zone dropped from 9.6% at the end of 2016 to 8.7% at the end of 2017, reaching the lowest level since January 2009. In Austria, it decreased from 5.7% to 5.3% over the same period. From August 2017 onwards, the rate of inflation in the euro zone remained constantly above 1.4%, with the average rate for the full year at 1.4% (after 1.1% in 2016). In Austria, the inflation rate rose significantly to 2.2% (2016: 1.0%). The rebound in inflation had limited impact on household purchasing power owing mainly to further acceleration in job creation. This consumer-led recovery has stimulated the business sector, leading to increased corporate profitability.[2]

Economic activity in the euro zone was resilient to political risks in 2017. The economic implications of the referendum in Catalonia in October 2017 were limited and the considerable delays in forming a government in Germany after the September 2017 elections had no economic consequences. The biggest risk for the euro zone continues to be related to Brexit and the possibility of the UK eventually leaving the EU without a deal and facing a legal void.

[1] European Commission's Winter 2018 Interim Economic Forecast, February 2018.
[2] Eurostat.

At its October 2017 meeting, the Governing Council of the European Central Bank (ECB) decided to extend its Asset Purchase Programme (APP) for another nine months until September 2018 at a reduced monthly pace of EUR 30bn in purchases (previously EUR 60bn/month) without any other changes to interest rates or to forward guidance. The ECB decided to keep its quantitative easing programme (QE) open-ended. The Council took stock of the further improvement of the economic situation, while stressing that the medium-term outlook for inflation, though also improving, was still a concern.[3]

At its December 2017 meeting, the Governing Council of the ECB kept interest rates on main refinancing operations and the deposit facility unchanged at 0.00% and minus 0.40%, respectively. The low-yield environment has furthermore supported the strong demand for fixed income products even at very low yields; the constant demand from QE buying has boosted debt capital market activities, especially in sovereign debt and covered bond markets, and led to constantly reduced volatilities and correlations across debt and equities markets.[4]

In the US, the Federal Reserve System (Fed) reacted to the positive data for employment and inflation by continuing the step-by-step normalisation of its monetary policy. It increased the key lending rate three times in 2017, most recently to a range of 1.25% to 1.50% in December 2017. Furthermore, the Fed began to gradually reduce its total assets. Following the decision to start unwinding QE in October 2017, the decline in the Federal Reserve's balance sheet will scale up until it reaches a maximum of USD 50bn per month in 2018.[5]

Austrian municipalities in 2017

Kommunalkredit is traditionally deeply rooted in the Austrian municipal sector, with cities and municipalities accounting for a major part of its historic portfolio (loans granted before the privatisation in autumn 2015). The bank is well-positioned in the Austrian market when it comes to infrastructure financing, financial advisory, funding and the administration of support programmes. Therefore, Kommunalkredit is very familiar with the financial condition of local authorities. Since 2005, it has been producing the annual "Municipal Finance Report" in cooperation with the Association of Austrian Municipalities and the Association of Austrian Cities and Towns as well as with the support of Statistics Austria. This publication provides a detailed overview of the revenues and expenses of all cities (excluding Vienna) and municipalities in Austria.

According to the 2017 Municipal Finance Report (accounting year 2016), the Austrian local authorities are in solid financial condition. The balance of revenues and expenses for 2016 was positive at EUR 1.72bn, the second highest value since the turn of the millennium. Having generated a surplus according to the Maastricht criteria of EUR 31.0m or 0.01% of the Austrian gross domestic product (GDP), the local governments (excluding Vienna) again met the zero-deficit target of the Austrian Stability Pact adopted in 2012. Municipal investments increased by 1.6% to EUR 2.19bn, remaining at the high level reached in previous years. The downward trend of municipal debt observed since 2011 continued throughout 2016 with a reduction by 1.1% to EUR 11.14bn.

[3] OeNB, Financial Stability Report 34.
[4] OeNB, Financial Stability Report 34.
[5] Board of Governors of the Federal Reserve System, Press Releases.

THE BUSINESS MODEL OF KOMMUNALKREDIT AUSTRIA AG

Infrastructure matters

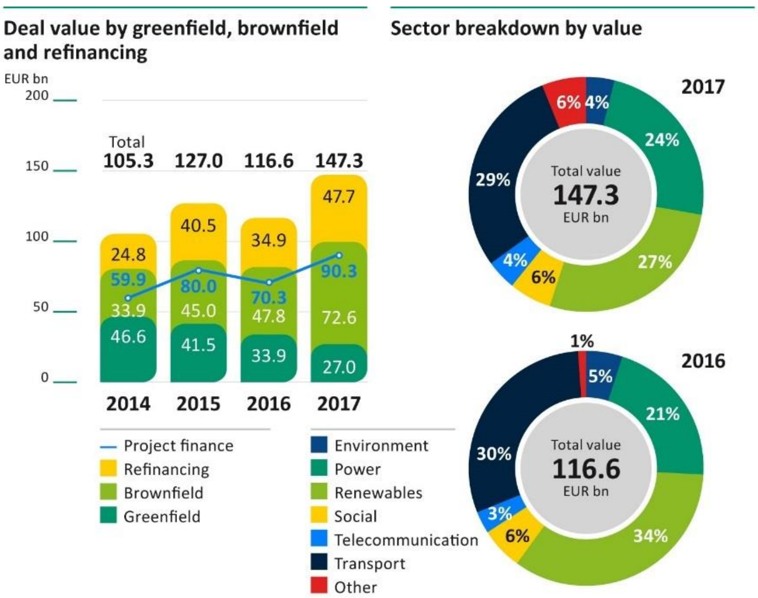
Infrastructure by its very nature is essential to the efficient functioning of society. Infrastructure investments can serve as a powerful tool for answering social needs and fundamentally increasing the general well-being of communities. They create the basis for prosperity and a high quality of life. Modern infrastructure is an indispensable prerequisite for the sustainable use of resources and successful approach to deal with climate change.

Demand for investment in infrastructure is enormous. The European Investment Bank (EIB) forecasts spending required to reach the targets of the Europe 2020 strategy at EUR 150bn to EUR 200bn per year.[6] Investment demand is particularly high in the sectors of energy, with a special focus on renewable energy, transport, social infrastructure and communications technology.

The way in which these projects are financed has changed significantly in recent years. As the financial latitude of the public sector is decreasing on account of the high level of government debt and budget caps, a shift from classic budget finance to project finance continues to occur thanks to private funding. In 2017, more than 60% of all infrastructure schemes in Europe were implemented through project finance.[7] Commercial banks continue to be a main source of debt for infrastructure projects. However, a host of other funders and products have appeared given the increasing acceptance of infrastructure as an asset class in its own right. Private placements, public bonds, direct institutional debt, multilaterals and export credit agencies are also heavily contributing to the sector. For institutional investors seeking stable long-term cash flows from a sustainable asset class, this offers an opportunity for real return enhancement in the current low-yield environment.

The European infrastructure market in 2017

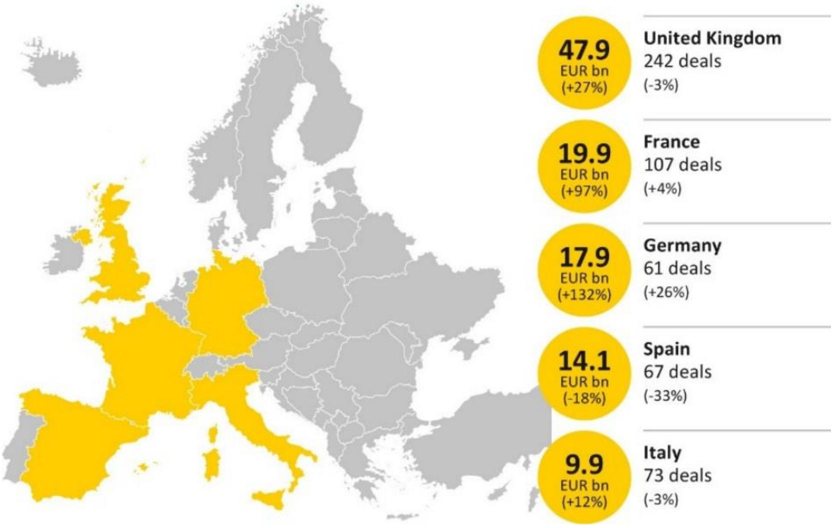
The European infrastructure market was booming in 2017, demonstrated, inter alia, by the significant increase by 26.3% in deal value to a total of EUR 147.3bn.[8] While the value of brownfield projects grew by 52% to EUR 72.6bn, a drop by 8% to EUR 27.0bn was observed in greenfield projects. The refinancing volume rose by 36.7% to EUR 47.7bn.



Source: Inframation. Based on a EUR-USD exchange rate of 1,19930.

[6] European Investment Bank, The Europe 2020 Project Bond Initiative – Innovative Infrastructure Financing, January 2017.
[7] Infrastructure information platform "Inframation".
[8] All figures in the section „The European infrastructure market in 2017" according to Inframation, based on a EUR-USD exchange rate of 1,19930.

The top 5 European infrastructure markets by deal value and number of deals



2017 experienced a strong inflow of equity from institutional investors and investment funds, with equity (including government grants) accounting for 38.7% of the total financing volume. In addition, the market saw a rise in the share of long-term private placements and capital market bonds. 12.6% of total volume were financed via capital market bonds,

while loans made up 48.7%.

Energy & environment (environment, power, renewables) accounted for 55% of total deal value, transport for 29%, social infrastructure for 6% and communications technology for 4%. As in 2016, the markets with the strongest demand were the United Kingdom (UK) with a financing volume of EUR 47.9bn, France (EUR 19.9bn), Germany (EUR 17.9bn), Spain (EUR 14.1bn) and Italy (EUR 9.9bn). Except for Spain, growth was recorded in all of these markets, especially in France and Germany. The positive development in the UK was particularly worth mentioning with an increase in volume by 27% despite the looming Brexit deadline, which has not discouraged investors from committing capital to UK's infrastructure.

Kommunalkredit's business model

We provide tangible benefit to the community

Kommunalkredit contributes to the sustainable success of infrastructure projects that improve the quality of peoples' life. The bank provides tangible benefit to the community in terms of economic dynamism, job creation, social cohesion, urban development and climate change.

By combining in-depth industry expertise and structuring know-how with the financing ability of a bank and strong relationships with international clients und investors, Kommunalkredit achieves strong impact for its clients and generates sustainable value for its stakeholders. The bank enables the implementation and operation of infrastructure, bridging the needs of project sponsors (developers and operators of infrastructure) and institutional investors, such as insurance companies, pension funds, banks, family offices and infrastructure funds. Kommunalkredit has established itself as a reliable partner for its key clients.

Backed by two international and long-term oriented shareholders, Kommunalkredit positions itself as a leading market player in the European infrastructure market, concentrating on energy & environment, social infrastructure & communications technology and transport.

Energy & Environment
- Energy supply & distribution
- Renewable energy
- Water supply & treatment
- Waste management & disposal

Transport
- Roads, bridges, tunnels
- Airports, ports, waterways
- Rail/light rail, rolling stock

Social Infrastructure & Communications Technology
- Nurseries, schools, universities
- Hospitals, nursing homes
- Police & court buildings
- Administrative buildings
- Broadband / Fibre Optic / Data Center

As a specialised bank, Kommunalkredit advises, structures and funds senior debt and mezzanine structures across the entire life cycle of an infrastructure project. Kommunalkredit's investments are focused on stable, cash flow-based, project secured transactions.

Kommunalkredit cooperates manifold with international institutions, such as the EBRD and the EIB.

SIGNIFICANT EVENTS OF THE BUSINESS YEAR

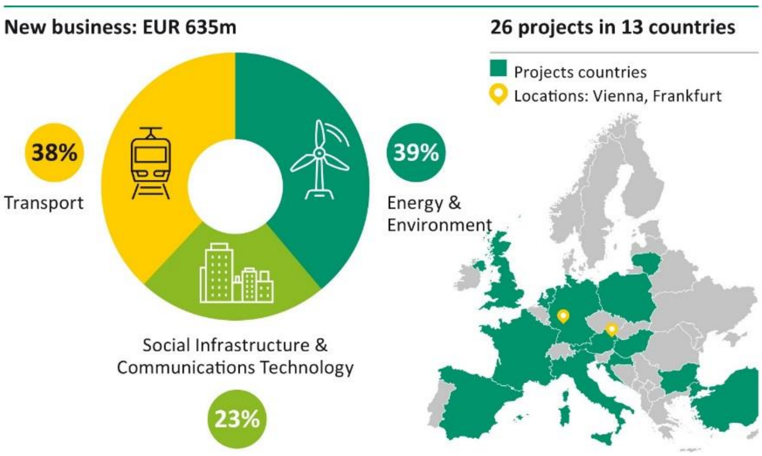
Business review

The bank is well on track to meet its growth targets, looking back on its best year in infrastructure finance so far. In 2017, Kommunalkredit generated a consolidated after-tax result of EUR 18.1m (IFRS). This result reflects the growing contribution from new business both to net interest income and fee and commission income. The bank invested in new strategic initiatives in 2017, such as the implementation of its new online retail platform KOMMUNALKREDIT INVEST, and strengthened its front office team. In parallel, it enacted a cost efficiency programme to streamline processes, which will lead to a reduction of the cost base in 2018.

1. Strong new business development: origination, execution, distribution

Significant growth with a diversified portfolio

Kommunalkredit managed to close 26 projects in 13 countries with commitments worth EUR 635.2m (2016: EUR 146.3m) delivering a P&L impact significantly above plan. The new business portfolio was highly diversified in terms of product, region and asset class with attractive risk/return profiles. It was distributed widely across various asset classes, with 13 projects and 39% of the total volume accounted for by the energy & environment segment (waste-to-energy, on-shore wind, solar), 6 projects and 38% of the volume by transport (roads, airports), and 6 projects and 23% of the volume by social infrastructure & communications technology (hospitals, nursing homes, fixed line/broadband). The total included one public-sector direct finance transaction. With 26 projects spread across 13 European jurisdictions, Kommunalkredit reached a high degree of regional diversification. Kommunalkredit provided finance for both brownfield projects (16 transactions) and greenfield projects (9 transactions). Thus, the steep growth in brownfield projects recorded in Europe in 2017 was reflected in the bank's new business.



Not only the bank's origination but also its distribution activities were highly diversified. Kommunalkredit placed new business worth EUR 194.2m for a total of 9 projects with a wide range of institutional investors across Europe. The successful distribution activity testifies to new business transactions' market conformity in terms of structure, pricing and risk management.

Flagship projects

Kommunalkredit contributed to implementing the financing of a number of notable projects, playing a leading role in half of the transactions either as Mandated Lead Arranger (11 projects) or Co-Arranger (2 projects). In the transport sector Kommunalkredit acted as Mandated Lead Arranger in the EUR 182m refinancing of the A21 Shadow Toll Road in Spain and in the EUR 230m refinancing of a section of the A2 Motorway in Poland. Furthermore, the bank was mandated as Joint Bookrunner and Underwriter in the EUR 1.2bn senior funding of the Superstrada Pedemontana Veneta, an Italian greenfield motorway, via a project bond.

A2 Section Toll Road (Poland)

Kommunalkredit acted as Joint Mandated Lead Arranger in the EUR 230m refinancing of the A2 section 1 Toll Road in Poland. The project was the first toll motorway to be designed, built, financed and operated under a concession-based model in Poland.

The first phase of the A2 involves construction, operation and maintenance of 149km of motorway between Konin and Nowy Tomyśl.

The A2 forms part of Poland's strategic Berlin – Warsaw corridor, providing one of the most important transportation links between Western and Central Europe. Traffic levels have continuously risen with an annual average growth rate of 12% since the opening of the motorway.

A21 Shadow Toll Road (Spain)

Kommunalkredit acted as Mandated Lead Arranger in the EUR 182m refinancing of the Spanish A21 Motorway. The project covers the refinancing of the operation and maintenance of six sections on the motorway. The A21 Autovía del Pirineo is a shadow toll road based on a 30-year concession-based model. Located in Navarra, the motorway is highly important for the region's transport network, running parallel to the Pyrenees at the border between Spain and France.

The project has substantial upside potential as adjacent motorways are expected to be constructed in the coming years. Navarra is one of the wealthiest regions in Spain, boasting the third highest GDP per capita and the lowest unemployment rate.

In the energy & environment segment, the bank contributed to various waste-to-energy deals, inter alia, acting as Mandated Lead Arranger in the EUR 240m financing of the Gipuzkoa plant in Spain and as Senior Lender in the primary syndication of the GBP 505m debt refinancing of the Cory Riverside facility in England, as well as in the GBP 179m financing of Parc Adfer in North Wales. Furthermore, the bank took part as Arranger and Senior Lender in the financing of solar and wind parks in France, Germany, Italy, Spain and the United Kingdom. Eventually, Kommunalkredit acted as Mandated Lead Arranger in the financing of the acquisition of a leading national fixed line telecoms operator in Southeastern Europe and took part in the financing of a nursing home in Germany.

Gipuzkoa Waste-to-Energy (Spain)

Kommunalkredit acted as Mandated Lead Arranger in the EUR 240m financing of the waste-to-energy plant in Spain. The project, implemented under a 35-year availability-based scheme, covers the design, construction, financing, operation and maintenance of the Gipuzkoa Environmental Complex in the Basque Region. The facility includes a mechanical-biological treatment plant, a waste-to-energy plant and auxiliary systems, utilities and ancillary equipment.

The project is of strategic importance to the region as waste is currently transported to be processed elsewhere, leading to costs and environmental inefficiency. The project is a viable alternative to improve the waste management system and reduce costs.

Bité Telecom (Baltics)

Kommunalkredit acted as Senior Lender in the EUR 105m refinancing of Bité, a leading telecoms operator in the Baltic region. Bité was acquired in 2016 by Providence Equity Partners to act as a consolidator in the Baltic telecoms and media markets.

The new facility is used to partially refinance Bité´s own acquisition debt as well as to provide additional funds for the acquisition of MTG Baltics, a leading Baltic TV & Media infrastructure group. The latter deal enables Bité to grow revenues and profit per existing customer as well as to gain market share. This project puts Kommunalkredit on the map both in the CEE region as well as in the communications technology/broadband sector, as evidenced by a number of follow-on transactions in 2017.

First industry awards

The bank's success is being recognised in the market. Kommunalkredit was awarded its first industry accolades in 2017. This included the Superstrada Pedemontana Veneta project, which was elected the "Europe Transport Deal of the Year" by the leading infrastructure journal *PFI,* and the Riverside transaction, which was ranked as one of the "Top 10 Infrastructure Deals" in 2017 by *Inspiratia*, another highly regarded infrastructure journal. In the league table of leading "bond arrangers" in Europe in 2017 published by *Inframation*, a renowned infrastructure platform, Kommunalkredit held 18th position.

PFI Europe Transport Deal of the Year
Superstrada Pedemontana Veneta (Italy)

Kommunalkredit acted as Joint Bookrunner and Underwriter in the EUR 1,2bn project bond financing of the Superstrada Pedemontana Veneta, an Italian greenfield motorway. The project covers the financing of the construction, the operation and maintenance of the motorway with a total length of 162km.

The Superstrada is of significant importance for the region's connection. Its main axis is 94km long and connects 34 municipalities as well as the main industrial areas of Vicenza and Treviso. It also includes the construction of 68km of secondary/access roads. The deal was chosen as the "Europe Transport Deal of the Year 2017" by the leading infrastructure journal *PFI*.

Inspiratia Top 10 Infrastructure Deals
Cory Riverside Waste-to-Energy (UK)

Kommunalkredit acted as Senior Lender in the GBP 505m debt refinancing of the Cory Riverside waste-to-energy plant in England. The facility has been operating at full capacity since its launch in 2012. In 2016 it processed 753,000 tonnes, with 60% of its waste derived from long-term supply contracts with municipal customers.

The plant is unique as it is river-based and London's waste is transported mainly on a fleet of barges, avoiding road transport. The waste is then turned into sustainable energy. This Riverside transaction was ranked as one of the "Top 10 Infrastructure Deals in 2017" by the highly regarded infrastructure magazine *Inspiratia*.

Collaboration between public entities and private partners as an efficient form of procurement

Against the background of the limited financial latitude allowed to public budgets, the collaboration between public entities and private partners offers an efficient and transparent form of procurement for the public sector. In such a cooperation the private partner (usually a special purpose company with significant private-investor participation) agrees to deliver a public infrastructure project and service under a long-term contract. The private partner assumes various project risks, notably with regard to designing, building, operating and financing the project. In practice, two models are widely used: The public authority either pays an availability fee to the private partner as soon as the infrastructure is available (availability-based model) or gives the private partner the right to generate revenues from the provision of the infrastructure (concession-based model).

In 2017, 68 greenfield projects with a value of EUR 13.8bn were implemented in Europe based on this type of partnerships compared to 48 projects with a value of EUR 10.3bn in 2016.[9] Kommunalkredit engaged in several projects, including the financing of both the Gipuzkoa waste-to-energy plant in Spain and the Parc Adfer facility in North Wales and, as Financial Advisor, in the implementation of the Berresgasse school project in Vienna (all availability-based). Furthermore, it took part in the refinancing of the A21 motorway in Spain and the A2 motorway in Poland as well as the financing of the Superstrada Pedemontana Veneta project (all concession-based).

Campus+ Berresgasse School (Austria)

Kommunalkredit acted as Advisor to an Austrian construction group in a bid for a City of Vienna availability-based model for the construction of the Campus+ Berresgasse school project. Kommunalkredit's mandate was to structure the senior debt financing, including an element of the EIB (EFSI) funding, and to tailor a financing model.

The City of Vienna is building a number of schools under its 2013-2023 programme for the construction of new educational facilities (BIENE), Campus+ Berresgasse being the third project implemented under the programme and the first relying on project finance – after Attemsgasse (on-balance) and Stammersdorf (leasing). The BIENE programme has an overall funding volume of about EUR 700m.

Parc Adfer North Wales Waste-to-Energy (UK)

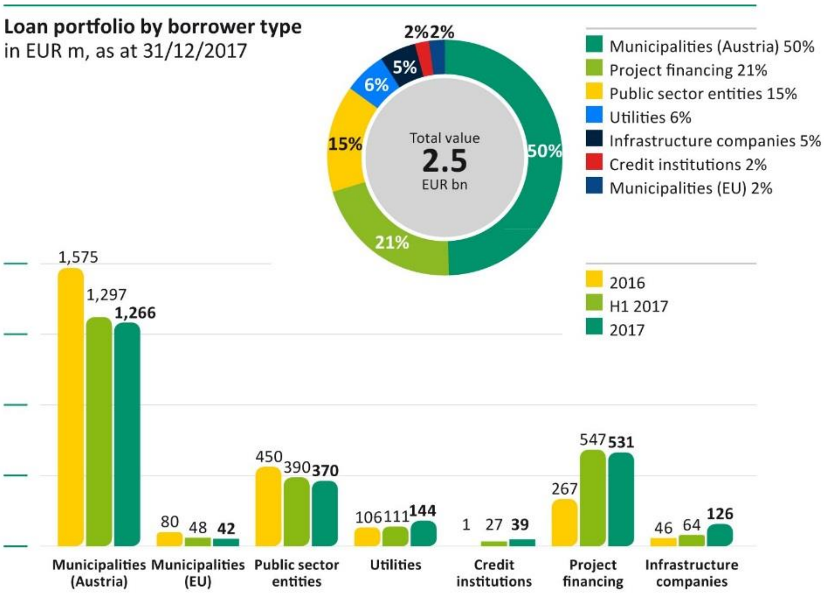
Kommunalkredit acted as Senior Lender in the EUR 179m financing of the Parc Adfer waste-to-energy plant. The facility, partly implemented under an availability-based scheme, is part of a project to manage waste in a more sustainable way in North Wales.

The construction of the plant with a 25-year operational life will be finished in 2019. The facility will have the capacity to deal with 200,000 tonnes of waste annually, with municipal waste accounting for 60% to 70% and merchant waste for 30% to 40%. The plant will supply 16MW of energy to the grid, while steam from the facility will be used to heat commercial and industrial businesses and residential areas in the region. Adfer, the name of the plant, means "to recover" in Welsh.

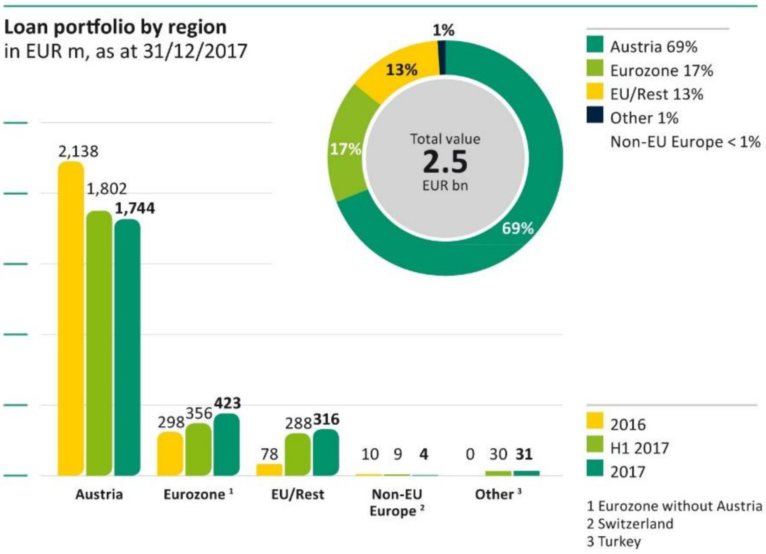
2. High quality of the loan portfolio

The bank holds a loan portfolio of high asset quality without a single default in the reporting year. As of 31 December 2017, the average rating was "A", with 89.4% of the loans being investment grade.

The non-performing-loan (NPL) ratio was maintained at 0.0% in 2017. The weighted average probability of default was 0.23%.



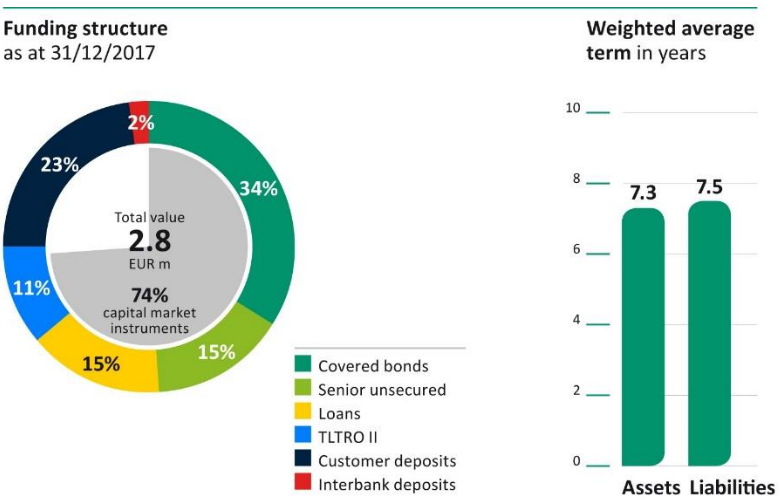
[9] Source: Inframation based on a EUR-USD exchange rate of 1,19930.



The loan portfolio is well-balanced with increasing project finance transactions and a prevalence of municipalities. As of 31 December 2017, municipalities accounted for 52% of the portfolio, with Austrian municipalities making up 50 percentage points. Project financing already accounted for 21%, while public sector enterprises had a share of 15%. Regionally, Austria contributed 69% to the loan portfolio, followed by the rest of the euro zone with 17% and other EU countries with 13%.

3. Funding position strengthened

As of 31 December 2017, Kommunalkredit continued to report a very strong liquidity position with a free liquidity reserve of EUR 283.1m (31/12/2016: EUR 390.4m). This included high-quality liquid assets (HQLA) in the amount of EUR 133.1m (31/12/2016: EUR 54.3m). Furthermore, EUR 150.0m (31/12/ 2016: EUR 336.1m) were eligible for funding via the ECB-tender or the General Collateral Pooling (GC Pooling).



In 2017, the bank succeeded in further strengthening its funding structure and broadening its investor base. Amounts owed to customers increased to a total of EUR 1,038.0m (31/12/2016: EUR 552.1m). This positive development was primarily driven by the tripling of customer deposits to EUR 644.4m (31/12/ 2016: EUR 210.8m).

Amounts owed to customers also included long-term private placements to customers of EUR 329.9m (31/12/2016: EUR 341.3m) and liabilities from collateral received in connection with derivatives of EUR 63.7m (31/12/2016: EUR 0.0m).

Kommunalkredit issued a EUR 300m social covered bond with a term of 4 years in 2017. This was the first emission of this asset class in Austria. Other capital market instruments, especially covered (34%) and senior unsecured bonds (15%), accounted for 74% of the bank's funding. The weighted average term of liabilities stood at 7.5 years, thus slightly exceeding the weighted average term of assets standing at 7.3 years.

Rising volume of customer deposits

- Retail deposits (KOMMUNALKREDIT INVEST): At the end of September 2017, Kommunalkredit launched its online retail platform KOMMUNALKREDIT INVEST in Austria as the bank's first move into retail business. KOMMUNALKREDIT INVEST takes sight deposits as well as term deposits for terms of up to ten years. By the end of 2017, the bank had attracted 1,900 retail customers with a deposit volume of EUR 115.7m (31/12/2016: EUR 0.0m). Since the beginning of January 2018, KOMMUNALKREDIT INVEST has also been operational in the retail market in Germany.

- Wholesale deposits (KOMMUNALKREDIT DIREKT and direct business with corporate customers): With its online platform KOMMUNALKREDIT DIREKT, the bank offers an efficient investment and cash management tool to municipalities and corporates. The strong growth seen throughout the year testifies to Kommunalkredit's close connection with its traditional municipal customer base in Austria. In addition, deposits by corporates rose significantly. In total, wholesale deposits more than doubled to EUR 528.8m as of 31 December 2017 (31/12/2016: EUR 210.8m). With an average volume of about EUR 2m, these deposits are highly granular, with a growing trend towards longer maturities.

Return to the capital market

In the second quarter of 2017, Kommunalkredit launched a Debt Issuance Programme (DIP) for medium-term notes (MTN), under which it placed a social covered bond with a volume of EUR 300m and a term of four years on 12 July 2017. This successful transaction marked Kommunalkredit's return to the capital market with its first public bond issue since its privatisation in 2015. The substantial investor interest was reflected in the order book, which was closed at EUR 530m, the issue being 1.8 times oversubscribed. In accordance with the general market environment, secondary market performance of the bond showed a spread tightening from mid swap +38bps at the time of issuance to approximately mid swap +30bps at year-end 2017.

Kommunalkredit was the first issuer of a publicly placed social covered bond in Austria, addressing the growing national and international demand for this investment category. About 50% of the investors are dedicated ESG[10] investors. In line with the green bond principles of the ICMA (International Capital Market Association), the net proceeds from the social covered bond issue are used to finance projects in the field of social infrastructure, i.e. education, health care and social housing, both for the funding of Kommunalkredit's existing social infrastructure portfolio and for new projects. As required, Sustainalytics, a leading sustainability rating agency, reviewed the implementation of the framework programme for social covered bonds at Kommunalkredit and confirmed all prerequisites for the issuance of the bond.

Besides the social covered bond issue, a first senior unsecured bond was sold as a private placement with an international investor in December 2017 within the framework of the successfully introduced Debt Issuance Programme.

[10] ESG = Environment Social Governance according to ICMA (International Capital Markets Association).

Buyback programme for CHF-denominated covered bonds

In May 2017, Kommunalkredit launched a buyback programme capped at CHF 200m addressing CHF 651.3m (outstanding as of 31/12/2016) covered bonds. This was to improve the currency structure in the cover pool (CHF denominated bonds vs. EUR assets; no currency mismatch in the bank). A volume of CHF 140.0m was tendered and accepted by the bank; this in combination with an ensuing 4-year EUR-denominated 300m newly issued covered bond achieved the targeted improvement. The enhanced profile was reflected in the covered bond rating. On 25 July 2017[11], Moody's upgraded the rating from "Baa2" to "Baa1", while S&P assigned an "A" rating to the newly issued EUR covered bond.[12]

Strong liquidity ratios

The Liquidity Coverage Ratio (LCR), which measures the short-term resilience of a bank's liquidity risk profile over a 30-day scenario, is closely monitored as part of the bank's early-warning system. With 449.9% as of 31 December 2017 (31/12/2016: 719.1%), the bank clearly exceeded the new regulatory minimum of 100% effective 1 January 2018.

The Net Stable Funding Ratio (NSFR), which, under Basel III, requires banks to maintain a stable funding profile in relation to the composition of its assets and off-balance sheet activities, stood at 101.5% as of 31 December 2017 (31/12/2016: 83.9%). The final definition of the ratio and associated implementation timeframe has not yet been confirmed by regulatory authorities.

4. Rating

Kommunalkredit's unsecured debt issues have a long-term rating of "BBB (low)" (negative trend) and a short-term rating of "R-2 (mid)" from the DBRS rating agency.

On 13 June 2017, Standard & Poor's assigned an "A" rating to Kommunalkredit's covered bonds, thus confirming the high quality of the underlying cover pool. Moody's assigned a "Baa1" rating to Kommunalkredit's covered bonds. On 24 November 2017, Kommunalkredit terminated its rating agreement with Moody's. Accordingly, the rating was withdrawn by Moody's on 14 December 2017. The rating agreement with S&P remains unchanged.

New appointments to the Executive Board and to the Supervisory Board

Effective 1 February 2017, Karl-Bernd Fislage was appointed to the Executive Board, assuming responsibility for Banking & Markets. The Executive Board consists of Alois Steinbichler, (Chief Executive Officer), Jörn Engelmann (Chief Risk Officer), Karl-Bernd Fislage (Banking & Markets) and Wolfgang Meister (Chief Operating Officer and Chief Financial Officer).

Effective 24 July 2017, Martin Rey, Managing Director of Maroban GmbH, was appointed as Member of the Supervisory Board. Werner Muhm resigned from his position as of 10 March 2017.

[11] Rating Action, 25 July 2017 by Moody's.
[12] RatingsDirect, 13 June 2017 by S&P.

OTHER MATERIAL DISCLOSURES

Service Agreement between Kommunalkredit and KA Finanz AG

Under the service agreement (SA), which has been in place since 2009, Kommunalkredit provides operational services for banking operations to KA Finanz AG. Kommunalkredit's expenses under the SA are charged to KA Finanz AG. In addition, as of 31 December 2017, 14 staff members were delegated to KA Finanz AG on a full-time basis, according to a staff leasing agreement.

In February 2018, KA Finanz AG has published a tender for services currently provided by Kommunalkredit. The bank intends to submit an offer for the continuation of such services. A decision by KA Finanz AG is expected by midyear 2018. Should the bank not be awarded with a continuing contract, the service contract with KA Finanz AG will expire in the first half of 2019. In such case the operative capacity will be adjusted during a contractually existing transition period of 12 months.

Corporate Governance and Risk Management

Kommunalkredit has a clear corporate governance and risk management structure.

Supervisory Board

In 2017, the Supervisory Board performed its tasks, as defined in the Articles of Association and the rules of procedure, within the framework of its ordinary and extraordinary meetings. Four regular Supervisory Board meetings, one extraordinary Supervisory Board meeting, two Audit Committee meetings, two Risk Committee meetings, two Nomination Committee meetings as well as one Remuneration Committee meeting were held in 2017.

Executive Board

The Executive Board of Kommunalkredit was enlarged to four members. The allocation of tasks and the procedures for cooperation within the Executive Board are determined in the rules of procedure of the Executive Board. The members of the Executive Board continuously exchange information among themselves and with staff members in executive positions reporting to them. The Executive Board provides the Supervisory Board with regular, timely and comprehensive information on all relevant issues of business development, including the risk position and risk management of the company and its material subsidiaries.

In addition, in the interest of good corporate governance, regular exchanges take place between the Chairman of the Supervisory Board and the Executive Board. These include in particular the definition of the company's strategy and information on the bank's performance and its risk management. The latter issues are regularly brought to the attention of the Chairman of the Risk Committee.

The agenda of the weekly Executive Board meetings comprises decision-making and reporting items, which are recorded in the minutes; follow-up items are agreed and strictly monitored.

Internal audit / Compliance and money laundering

Internal Audit reports monthly to the Executive Board and submits quarterly reports directly to the Supervisory Board. Apart from ongoing contacts within the framework of day-to-day business, compliance submits semi-annual written reports to the Executive Board. The compliance officer also acts as anti-money-laundering officer pursuant to § 23(3) of the Financial Markets Money Laundering Act (*FM-GwG – Finanzmarkt-Geldwäschegesetz*) and, as such, is responsible for measures to ensure compliance with the provisions of the Financial Markets Money Laundering Act, in particular the duties of diligence vis-à-vis customers as laid down in §§ 5ff. The semi-annual AML and compliance reports are also submitted to the Supervisory Board.

Capital Adequacy

In accordance with the agreed allocation of tasks, the members of the Executive Board share the responsibility for ICAAP (Internal Capital Adequacy Assessment Process). ICAAP is a core element of Pillar 2 of the Basel Accord, comprising all procedures and measures applied by a bank to secure appropriate identification, measurement and limitation of risks, a level of capitalisation in line with the risk profile of the business model, and the use and continuous further development of suitable risk management systems.

Kommunalkredit uses a detailed risk-bearing-capacity analysis for the quantitative assessment of its capital adequacy. Depending on the target pursued, three different control loops are applied:

- Regulatory control loop
- Economic control loop (liquidation perspective)
- Going-concern control loop

Furthermore, regular stress tests are performed to test the robustness of the business model and to ensure the adequacy of the bank's capitalisation.

The risk management and ICAAP methods of the bank are reviewed annually. The monthly meetings of the Risk Management Committee (RMC) deal with credit, liquidity, market, operational and other risks on the basis of comprehensive reports. Other committees dealing with credit, capital and liquidity issues meet at least once a week (see also Notes to the Consolidated Financial Statements of the Kommunalkredit Group).

ASSETS, FINANCIAL POSITION AND INCOME

Financial performance indicators of Kommunalkredit Group according to IFRS

Selected balance sheet figures in EUR m	31/12/2017	31/12/2016
Total assets	3,663.2	3,790.8
Loans and advances to customers	2,091.9	2,138.9
Assets at fair value	605.7	691.6
Assets available for sale	211.6	147.0
Amounts owed to banks	532.8	795.0
Amounts owed to customers	1,038.0	552.1
Securitised liabilities	1,468.6	1,779.2
Equity	283.1	296.8

Selected income statement figures in EUR m	1/1-31/12/2017	1/1-31/12/2016
Net interest income	35.2	36.5
Net fee and commission income	17.3	16.8
Loan impairment for incurred but not reported losses	-0.3	0.1
General administrative expenses	-58.6	-49.3
of which new strategic initiatives	*-3.0*	*-0.5*
of which efficiency programme	*-2.7*	*0.0*
Other operating result	11.2	-0.1
of which services provided to KA Finanz AG	*12.1*	*10.9*
of which stability tax	*-0.7*	*-11.6*
Contributions to the Bank Resolution Fund	-0.9	-2.5
Net trading and valuation result	3.1	36.2
Taxes on income	11.0	13.5
Consolidated profit for the year after tax	18.1	49.0
Comprehensive income (incl. changes in equity)	18.4	48.6

Key indicators in EUR m or%	31/12/2017	31/12/2016
Risk weighted assets	992.4	686.1
Total capital ratio	29.9%	42.3%
Common equity tier 1 after dividend	233.0	225.5
CET 1 ratio	23.5%	32.9%
Return on equity after tax (Consolidated profit for the year after tax / common equity tier 1 as of 1/1 current fiscal year)	8.0%	25.2%
Cost/income ratio Kommunalkredit Group*	89.5%	71.3%

*Net general administrative expenses after services invoiced to KA Finanz AG relative to interest income, fee and commission income, loan impairment for incurred but not reported loss and other operating result (not including income from services provided to KA Finanz AG and stability tax)

Rating	31/12/2017	31/12/2016
Long-term DBRS	BBB (low)	BBB (low)
Short-term DBRS	R-2 (mid)	R-2 (mid)
Covered Bonds S&P	A	-

Balance sheet structure

As of 31 December 2017, Kommunalkredit's total assets stood at EUR 3.7bn (31/12/2016: EUR 3.8bn), under IFRS. Total assets included loans and advances to customers worth EUR 2.2bn (recognised under loans and advances to customers and assets at fair value through profit or loss; 31/12/2016: EUR 2.4bn). The securities portfolio (recognised under loans and advances to customers, assets at fair value and assets available for sale) stood at EUR 584.8m (31/12/2016: EUR 560.8m) and included high-quality liquid assets (HQLA) in the amount of EUR 133.1m (31/12/2016: EUR 54.3m).

The structure of liabilities according to IFRS book values is as follows:

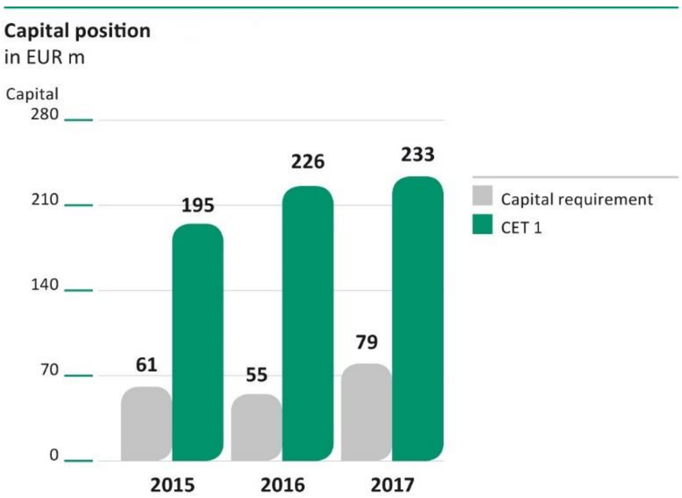
Structure of liabilities 31/12/2017 and 31/12/2016 in EUR bn	31/12/2017	31/12/2016
Securitised liabilities	1.5	1.8
Amounts owed to customers	1.0	0.6
Amounts owed to banks, including ECB	0.5	0.8

As in previous years, the bank's main funding components were senior and covered bonds reported under securitised liabilities worth EUR 416.7m and EUR 965.3m respectively (31/12/2016: EUR 474.8m and EUR 1.34bn respectively).

Amounts owed to customers increased to a total of EUR 1,038.0m in 2017 (31/12/2016: EUR 552.1m), comprising customer deposits of EUR 644.4m (31/12/2016: EUR 210.8m), long-term private placements to customers of EUR 329.9m (31/12/2016: EUR 341.3m) and liabilities from collateral received in connection with derivatives of EUR 63.7m (31/12/2016: EUR 0.0m). Amounts owed to banks primarily comprised funds drawn under the long-term tender programme (TLTRO-II) of the European Central Bank (ECB) in the amount of EUR 313.9m (31/12/2016: EUR 313.9m), deposits by banks in the amount of EUR 43.0m (31/12/2016: EUR 20.0m) as well as liabilities from collateral received for derivatives of EUR 96.2m (31/12/2016: EUR 216.5m).

Risk-weighted assets and regulatory own funds

As of 31 December 2017, Kommunalkredit's own funds totaled EUR 297.2m (31/12/2016: EUR 290.3m) and its common equity tier 1 capital (CET 1) stood at EUR 233.0m (31/12/2016: EUR 225.5m). During the reporting period of 2017, risk-weighted assets increased by 44.6% to EUR 992.4m (31/12/2016: EUR 686.1m) owing to a higher weighting of new business in infrastructure project finance compared to the decreasing portfolio with mostly Austrian public entities.



As of 31 December 2017, Kommunalkredit thus reported a total capital ratio of 29.9% (31.12.2016: 42.3%) and a CET 1 ratio of 23.5% (31/12/2016: 32.9%). The leverage ratio stood at 7.3% as of 31 December 2017 (31/12/2016: 7.2%).

Kommunalkredit has to comply with the own funds requirements as stipulated in article 92 CRR and the related Supervisory Review and Evaluation Process (SREP). Under these parameters Kommunalkredit had to maintain a minimum CET 1 ratio of 6.05%, a minimum core capital ratio of 7.65% and a minimum total capital ratio of 9.85% as of 31 December 2017; these ratios are significantly exceeded by the bank.

The foregoing figures reflect the regulatory capital indicators based on the unconsolidated financial statements of Kommunalkredit pursuant to the Austrian Company Code/Austrian Banking Act as reported in the financial statements for 2017. Equity already reflects a dividend of EUR 11.5m., which the Executive Board will propose at the annual shareholders' meeting for the business year 2017.

Kommunalkredit is also part of a group of credit institutions whose parent is Satere Beteiligungsverwaltungs GmbH (Satere). As of 31 December 2017, the consolidated total capital ratio shows 29.2% (31.12.2016: 42.3%), the consolidated CET 1 ratio shows 22.8% (31/12/2016: 32.9%).

Public sector covered bonds / Cover pool

As of 31 December 2017, Kommunalkredit had a well-diversified cover pool with a nominal value of EUR 1.3bn. At the same time, EUR- and CHF-denominated public-sector covered bonds in the nominal amount of approx. EUR 965m were outstanding. As of 31 December 2017, the cover pool comprised assets from Austria (96.9%), Germany (2.0%) and Poland (1.2%); 80.6% of the cover pool was rated "AAA" or "AA"; 19.4% of the cover pool assets had an "A" rating.

For its covered bonds in circulation, Kommunalkredit committed itself to maintaining a voluntary nominal over-collateralisation of approx. 10% of the redemption amount. As of 31 December 2017, the level of over-collateralisation was 30.3%.

Profit & Loss Account of the Group according to IFRS

In 2017, Kommunalkredit Group generated a consolidated IFRS after-tax result of EUR 18.1m (2016: EUR 49.0m). The decrease compared to the previous year resulted mainly from one-off positive effects relating to the buyback of own issues not materialising to the same extent as in 2016. This, however, was fully in line with expectations and budget. The 2017 result reflects the growing volume of new business positively contributing to net interest income as well as fee and commission income. In addition, the bank invested in new strategic initiatives, in particular in the launch of its new online retail platform KOMMUNALKREDIT INVEST. The front office team was strengthened by hiring highly experienced experts with a strong international track record. In parallel, Kommunalkredit enacted a cost efficiency programme to streamline processes, which will lead to a reduction of the cost base in 2018.

The material income and expense items of the consolidated IFRS financial statements for 2017 are as follows:

- **Net interest income**
  Net interest income declined by 3.6% to EUR 35.2m (2016: EUR 36.5m). The significant increase of the contribution from new business to EUR 7.9m (2016: EUR 0.2m) almost fully compensated for the reduction due to scheduled maturities in the existing portfolio.

- **Net fee and commission income**
  Net fee and commission income increased by 2.8% to EUR 17.3m (2016: EUR 16.8m). It resulted from fees and commissions earned by KPC in its support programme management and consulting activities in the amount of EUR 16.0m (2016: EUR 17.0m) as well as income from the banking business of EUR 1.3m (2016: EUR -0.2m). In total, the bank received arrangement fees in the amount of EUR 10.2m in 2017. According to IFRS rules, EUR 1.2m carried through profit or loss, whereas an amount of EUR 9.0m was recognised as a component of the effective interest rate and will strengthen future interest income.

- **Net provisioning for impairment losses**
  The non-performing-loan (NPL) ratio (definition of default according to Basel III) remained at 0.0%. No loan defaults were recorded in 2017. The loan impairment charge of EUR -0.3m reported for 2017 (2016: EUR 0.1m) reflects the addition to the portfolio loan loss provision according to IAS 39 for "incurred but not reported losses".

- **General administrative expenses**
  General administrative expenses rose by 18.9% to EUR 58.6m (2016: EUR 49.3m), comprising personnel expenses of EUR 38.8m (2016: EUR 31.5m) and other administrative expenses of EUR 19.8m (2016: EUR 17.9m). The increase in general administrative expenses was mainly due to the following factors:
  - Strengthening of the front office team through experienced experts with an international track record;
  - Investments of EUR 3.0m in new strategic initiatives such as the online retail platform KOMMUNALKREDIT INVEST;
  - Expenses of EUR 2.7m in relation to a cost efficiency programme to streamline operational processes;
  - Expenses of EUR 0.5m to implement new regulatory requirements (e.g. MiFiD 2, IFRS 9).

- **Other operating result**
  The position other operating result increased by EUR 11.3m to EUR 11.2m (2016: EUR -0.1m). The main component of other operating income is the revenue generated from the provision of operational services for KA Finanz AG in an amount of EUR 12.1m (2016: EUR 10.9m). The expenditure for the stability tax payable by Austrian banks dropped significantly to EUR 0.7m in 2017, as compared to EUR 11.6m in the previous year. In 2016, Kommunalkredit had decided to make a non-recurrent special payment of EUR 7.7m, which resulted in a substantial reduction of the stability tax expense for the business years from 2017 onwards.

- **Contribution to bank resolution fund and stability tax**
  The contribution to the bank resolution fund for 2017 amounted to EUR 1.7m. After the release of accruals of EUR 0.8m, the negative impact on earnings amounted to EUR 0.9m (2016: EUR 2.5m).

- **Net trading and valuation result**
  The net trading and valuation result amounted to EUR 3.1m (2016: EUR 36.2m). The decrease compared to the previous year was primarily due to the fact that as expected, positive one-off effects from the buyback of own issues did not occur to the same extent in 2017 (EUR 6.3m in 2017 compared to EUR 48.1m in 2016).

- **Taxes on income**
  The income tax item for 2017 is positive at EUR 11.0m (2016: EUR 13.5m). This is due, above all, to the capitalisation of tax loss carry-forwards on the basis of current tax budgeting in accordance with IFRS rules.

Profit & Loss Account of Kommunalkredit Austria AG according to Austrian GAAP

Selected income statement figures in EUR m	1/1-31/12/2017	1/1-31/12/2016
Net interest income	32.8	36.2
Net fee and commission income	8.5	0.6
General adminstrative expenses	-45.7	-38.7
Other operating income	23.7	14.0
of which income from services provided to KA Finanz AG & Kommunalkredit Public Consulting	*14.1*	*13.2*
of which income from the transfer of real estate assets	*8.6*	*0.0*
Other operating expenses	-0.7	-11.6
of which stability tax	*-0.7*	*-11.6*
Operating result	**18.6**	**0.7**
Loan impairment, valuation and sales result	8.4	54.8
Appropriation to provision (§ 57 (1) Austrian Banking Act)	-3.8	0.0
Profit on ordinary activities	**18.3**	**55.5**
Appropriation to the fund for general banking risks (§ 57 (3) Austrian Banking Act)	0.0	-25.0
Taxes on income	-0.1	7.0
Profit for the year after tax	**18.9**	**37.5**

The unconsolidated financial statements of Kommunalkredit Austria AG prepared in accordance with Austrian GAAP showed an operating result of EUR 18.6m for 2017 (2016: EUR 0.7m). This figure reflects the growing new business volume, which also led to rising interest and fee and commission income. Furthermore, the bank invested in new strategic initiatives, in particular in the launch of its new online retail platform KOMMUNALKREDIT INVEST. The front office team was strengthened through the recruitment of experienced experts with an international track record. In parallel, Kommunalkredit enacted a cost efficiency programme to streamline operational processes and the structure of the companies holding its participations.

Profit on ordinary activities totalled EUR 18.3m in 2017 (2016: EUR 55.5m), while after-tax profit for the year amounted to EUR 18.9m (2016: EUR 37.5m). The decrease compared to the previous year resulted mainly from the fact that as expected, one-off positive effects relating to the buyback of own issues not materialising to the same extent as in 2016. As in the previous year, the loan impairment charge of EUR -0.3m reported for 2017 (2016: EUR 0.1) is solely due to the changes to the general loan loss provision. No loan defaults were recorded in 2017. Kommunalkredit's non-performing-loan (NPL) ratio (definition of default according to Basel III) remained at 0.0%. The appropriation to the general risk provision pursuant to § 57 (1) of the Austrian Banking Act amounted to EUR 3.8m (2016: EUR 0.0m).

As of 31 December 2017, total assets according to Austrian GAAP remained at EUR 3.3bn, almost unchanged from the previous year, with loans and advances to customers of EUR 2.4bn (31/12/2016: EUR 2.6bn) and bonds and debt securities worth EUR 0.3bn (31/12/2016: EUR 0.2bn) accounting for the major part thereof.

Capitalisation – Dividend policy

Kommunalkredit since its privatisation in 2015 has enjoyed a very strong capital position. At year end 2017 this reflects a capital ratio of 29.9% with a CET 1 ratio of 23.5%. This is based on EUR 233.0m paid-in capital and capital reserves as well as EUR 64.2m tier 2 capital. As of 31 December 2017, the available capital exceeded the regulatory requirement by EUR 199.4m based on RWAs of EUR 992.4m. The bank has been investing excess capital in the build-up of new business; in the medium term a core capital ratio of around 15% is targeted. The foregoing capital position already reflects the dividend of EUR 11.5m, which the Executive Board will propose at the annual shareholders' meeting for the business year 2017.

The shareholders support the bank's strategy and growth plans to position Kommunalkredit as a leading player in the European infrastructure market. There are no predefined exit horizons for the shareholders' investment in Kommunalkredit. It is anticipated that additional capital will be available to support the bank's growth strategy. This also is evidenced by the availability of EUR 79.7m authorised capital implemented at the annual shareholders' meeting in March 2017.

NON-FINANCIAL PERFORMANCE INDICATORS

Employees

The average headcount of the Kommunalkredit Group in 2017 was 290 FTEs (full-time equivalents); thereof 183 in Kommunalkredit Austria AG, 91 in Kommunalkredit Public Consulting. 16 staff members were working on a full-time basis exclusively for KA Finanz AG, according to a staff leasing agreement. Kommunalkredit in addition provided operational services for KA Finanz AG under a service agreement (SA). As of 31 December 2017, the year-end headcount of Kommunalkredit Austria AG, excluding delegates to KA Finanz AG, was 182 FTE (31/12/2016: 178 FTE), including new hires, especially in Banking & Markets. In parallel, the bank enacted a cost efficiency programme which will lead to a reduction in headcount during the first half of 2018. Related expenses of EUR 2.7m are included in personnel expenses in 2017.

In 2017, 48% of the employees of the Kommunalkredit Group were female, who also held 38% of executive positions. The average age of employees was 41. The percentage of university graduates remained high at 65%. As of 31 December 2017, 15 female employees and five male employees were on parental leave. In 2017, three male employees took paternity leave and another three took advantage of the so-called "Papamonat" provision included in the collective labour agreement for banks as of 1 July 2011, which allows new fathers to stay at home for one month after the baby's birth, and the so-called "family time" provision for children born as of 1 March 2017 respectively.

The remuneration policy and practice of the Kommunalkredit Group is fully in line with the legal requirements for variable remuneration in banks pursuant to § 39b of the Austrian Banking Act and Art. 450 CRR, including the implementation of a "Remuneration Committee" of the Supervisory Board.

Communication

Kommunalkredit communicates actively and transparently with its stakeholders – the community, customers, business partners, investors, employees, regulatory authorities and shareholders. To engage in dialogue with its stakeholders, Kommunalkredit employs a broad range of communication tools. These include various forms of personal communication as well as digital media, classic public relations and direct marketing. Consistency in the bank's internal and external communication is ensured by the Corporate Communications unit.

In its external communication activities, Kommunalkredit in 2017 focussed on intensifying its presence in the media, both in the Austrian business media and in the international infrastructure press, and on promoting its two online investment platforms, KOMMUNALKREDIT DIREKT (for local authorities and corporates) and KOMMUNALKREDIT INVEST (for retail customers).

In Austria, Kommunalkredit has positioned itself as a knowledge platform for infrastructure and the municipal sector. It has developed a range of communication formats to address its main target groups, above all project sponsors with an emphasis on municipalities and institutional investors. One of the communication highlights in 2017 was the "Municipal Summer Symposium", a municipal-policy forum, which Kommunalkredit organised for the twelfth time in cooperation with the Association of Austrian Municipalities in 2017. In addition, Kommunalkredit presented the "Municipal Finance Report", which offers a detailed overview of the revenues and expenses of all cities and municipalities in Austria. The report has been published by the bank in close cooperation with the Association of Austrian Municipalities and the Association of Austrian Cities and Towns since 2005.

In its internal communication, Kommunalkredit makes every effort to ensure a transparent flow of information within the company. The bank uses a broad range of communication channels, from internal road shows to town hall meetings to communication via the intranet and the Kommunalkredit Academy, an internal portal with a variety of training options. The activities of the Sustainability Team and the Staff Council complement the active exchange of information.

To support its capital market activities, the Investor Relations unit intensified its direct contacts and conversations with investors and rating agencies, providing regular and transparent information about Kommunalkredit's development. Investor relations activities focused, above all, on the organisation of national and international roadshows as well as preparations for Kommunalkredit's return to the capital market with the social covered bond issue on 12 July 2017. These measures served to broaden the bank's stable base of investors and other stakeholders.

BRANCH OFFICES

As of 31 December 2017, Kommunalkredit had a branch office in Frankfurt am Main, Germany.

RESEARCH AND DEVELOPMENT

Given the sector in which the company operates, statements on research and development do not apply.

SIGNIFICANT EVENTS AFTER THE BALANCE SHEET DATE

Online retail platform KOMMUNALKREDIT INVEST also launched in Germany

At the beginning of January 2018, Kommunalkredit also introduced its online retail platform KOMMUNALKREDIT INVEST in Germany. KOMMUNALKREDIT INVEST offers sight deposits as well as term deposits for terms of up to ten years.

Services for KA Finanz AG

In February 2018, KA Finanz AG published a tender for services currently provided by Kommunalkredit. The bank intends to submit an offer for the continuation of such services. A decision by KA Finanz AG is expected by midyear 2018. Should the bank not be awarded with a continuing contract, the service contract with KA Finanz AG will expire in the first half of 2019. In such case the operative capacity will be adjusted during a contractually existing transition period of 12 months.

IFRS 9

As of 1 January 2018, the new IFRS 9 accounting standard introducing new rules on the recognition and valuation of financial instruments (loans, securities etc.) has come into effect. Kommunalkredit applies the new rules according to the standard; first adoption of IFRS 9 is expected to result in an increase in IFRS equity by approx. EUR 10m to around EUR 294m compared to 31 December 2017.

PARTICIPATIONS

Kommunalkredit Austria AG holds investments in various affiliated companies. Strategic holdings include Kommunalkredit Public Consulting (KPC) and Kommunalnet, whereas TrendMind and affiliated companies associated with our real estate assets (serving as headquarter) are mainly owned to support the bank's core business. The bank's regulatory capital tied up in participations totalled EUR 3.5m as of 31 December 2017.

Participations of Kommunalkredit Group				Financial statement disclosures (IFRS)			
Name and registered office	Investment direct	Investment indirect	Extent of investment in%	Most recent financial statements	Total assets in EUR 1,000	Equity in EUR 1,000	Profit/loss for the year in EUR 1.000
1. Affiliated companies							
1.1. Fully consolidated affiliated companies							
Kommunalkredit Public Consulting GmbH (KPC), Vienna	x		90.00%	31/12/2017	7,235.4	1,695.2	420.3
Kommunalkredit KBI Immobilien GmbH	x		100.00%	31/12/2017	34.9	34.9	-0.1
Kommunalkredit KBI Immobilien GmbH & Co KG	x		100.00%	31/12/2017	32,081.4	32,081.4	0.0
Kommunalkredit TLI Immobilien GmbH & Co KG		x	100.00%	31/12/2017	32,057.2	32,019.0	-45.4
1.2. Other investments of the AFS category							
TrendMind IT Dienstleistung GmbH (TrendMind), Vienna[1]	x		100.00%	31/12/2017	534.3	407.0	156.0
2. Associates							
2.1. Associates included at equity							
Kommunalleasing GmbH (Kommunalleasing), Vienna	x		50.00%	31/12/2017[2]	81,191.2	5,187.0	126.6
2.2. Other investments on the AFS category							
Kommunalnet E-Government Solutions GmbH (Kommunalnet), Vienna[1]	x		45.00%	31/12/2017[2]	1,300.1	1,032.2	166.7

[1] Values according to Austrian Company Code
[2] Preliminary unaudited figures

Kommunalkredit Public Consulting GmbH (KPC)

Kommunalkredit Public Consulting (KPC) is a service provider specialised in

- the management of public support programmes and
- consultancy services for national and international organisations and financial institutions in the area of environments and energy efficiency.

Management of support programmes

In 2017, KPC disbursed support grants in the amount of EUR 416.1m on behalf of the funding authorities, in particular the Federal Ministry of Agriculture, Forestry, Environment and Water Management, a long-time partner of KPC (renamed since 08/01/2018: Federal Ministry of Sustainability and Tourism), and the Austrian Climate and Energy Fund. The total volume of investments supported by such public grants was EUR 2,226.9m. KPC managed support initiatives in the areas of energy supply, energy conservation, water management, the remediation of contaminated sites, transport and e-mobility, as well as transactions under the "crafts bonus" scheme. Across all segments, 88,190 projects were approved and nearly 89,700 projects were settled in 2017, including 55,820 in the "crafts bonus" programme alone.

Projects processed and cleared by KPC in 2017 Amounts in EUR m	Projects assessed	Total capital expenditure	Support granted	Projects cleared	Disbursements
Federal environmental support schemes	**14,911**	**1,638.5**	**336.2**	**17,207**	**584.4**
Water management	1,627	527.6	94.6	1,298	341.1
Environmental support in Austria	4,683	547.3	67.8	4,666	64.0
Consultancy services	2,029	4.3	1.2	2,029	1.2
Renovation support for businesses	194	38.3	6.0	258	11.5
Renovation support for private households	5,557	196.3	19.4	8,157	28.2
Remediation of contaminated sites	10	25.5	23.5	13	44.4
Protective water management	602	181.2	97.3	740	91.3
klimaaktiv mobil	14	2.3	0.2	10	0.2
Funding for international climate projects	5	0.9	0.9	15	2.5
EU co-financing (Environmental Support Act)	190	114.7	25.0	21	0.0
Climate and Energy Fund	**16,438**	**349.6**	**53.1**	**15,620**	**46.6**
Photovoltaics	7,375	88.4	9.5	6,890	8.8
Wood-fired heating and solar installations	5,675	80.5	7.0	5,330	6.6
Mobility management	2,453	97.2	11.7	2,412	9.9
Employment programmes	351	30.4	16.7	336	21.2
EU co-financing	584	53.0	8.2	652	0.0
Other programmes	**56,841**	**238.8**	**26.8**	**56,841**	**24.3**
Green electricity – hydro power plants	12	42.6	1.6	47	0.0
Crafts bonus *	55,820	154.1	22.9	55,820	22.9
e-mobile Lower Austria	396	11.4	0.5	396	0.5
Salzburg Climate and Energy Pact	72	4.1	0.6	110	0.7
E-mobility in Styria	126	3.5	0.1	126	0.1
Cool businesses in Styria	4	0.7	0.2	0	0.0
Add-on funding Tyrol	301	17.6	0.7	252	0.0
Add-on funding Vorarlberg	65	4.0	0.2	54	0.1
Photovoltaics Vienna	45	0.8	0.1	36	0.0
Total	**88,190**	**2,226.9**	**416.1**	**89,668**	**655.4**

*short-term measure

Rounding differences may result from presentation in EUR million.

Consulting

In the year under review, KPC continued to broaden its range of consultancy services for national partners and international organisations and financial institutions. In its international consulting activities, KPC continues to focus on development cooperation, especially with countries in South Eastern, Central and Eastern Europe. KPC's renowned consultancy clients include the European Commission, the European Bank for Reconstruction and Development (EBRD), the World Bank, the Organisation for Economic Cooperation and Development (OECD) and the German Kreditanstalt für Wiederaufbau (KfW), as well as the Austrian and German development agencies.

KPC was awarded attractive new contracts in 2017. KfW, for example, commissioned a project for the "Reconstruction and Renovation of Municipal Infrastructure and Accommodation for Refugees". The objective of the project is to identify measures relating to water, waste and energy efficiency in Eastern Ukraine, which can subsequently be financed by KfW. Despite fierce international competition, a KPC-led consortium won the tender for the implementation of the Western Balkans Green Economy Financing Facility (WB GEFF – Residential) of the EBRD. The "Water Sector Framework – Regionalisation" project, concerning the organisation of the water sector in Belarus was also awarded by the EBRD.

Consulting activities relating to the international carbon market and to climate finance are an important priority for KPC. From 2003 to 2013, KPC managed the purchase of CO_2 emission allowance certificates from international climate action projects on behalf of the Republic of Austria, the objective being to achieve the Austrian Kyoto target. KPC is able to use its expertise in international climate action developed over the years for the benefit of other consultancy mandates, such as the World Bank (The Pilot Auction Facility for Methane and Climate Change Mitigation) and KfW (management of the "Future of the Carbon Market" Foundation). The Federal Ministry of Agriculture, Forestry, Environment and Water Management awarded consultancy services for the international climate negotiations to KPC.

Since 2008, KPC has also been running the "Climate Austria" programme, a platform for the voluntary compensation of CO_2 emissions, e.g. from travel, in cooperation with numerous private companies. KPC's ISO certification for its consulting business was re-confirmed in 2017.

Kommunalnet E-Government Solutions GmbH

Kommunalnet E-Government Solutions GmbH (Kommunalnet) is a 45% subsidiary of Kommunalkredit, the remainder being held by the Association of Austrian Municipalities (45%) and three of its regional organisations (10%). Kommunalnet is the digital work and information portal of Austrian local authorities, mayors and municipal staff. The platform offers current news for local authorities, provides access to relevant official databases, and serves as an information and communication hub between the federal, provincial and local government levels. Kommunalnet is an official component of the Austrian e-government road map.

Numerous projects were launched and implemented in 2017. The purpose of these projects is to support local authorities in their daily work, expand the scope of Kommunalnet's operations and utilise its potential for further growth. The main projects concern the expansion of the digital purchase platform "GEMEINDE DEALS", offering over 80,000 office supplies, the implementation of the e-Academy and the launch of e-procurement.

As of 31 December 2017, Kommunalnet had 13,422 registered users from 2,052 Austrian local authorities and associations of local authorities. Thus, Kommunalnet has an exceptionally high market-penetration rate of 95.8% in the municipal sector and holds a unique position in the Austrian market.

TrendMind IT Dienstleistung GmbH

TrendMind IT Dienstleistungen GmbH (TrendMind) is the IT specialist for financial products, SAP and software for support programme management. The company benefits from many years of experience with the implementation of SAP projects and internet solutions with a special focus on databases and financial products. The company's service portfolio includes not only classic software development activities, but also consultancy and technical project management services. In these fields, the company provides operational and maintenance services mainly for customers in Austria and Germany. TrendMind made a significant contribution to the success of the online retail platform KOMMUNALKREDIT INVEST.

Kommunalkredit TLI Immobilien GmbH & Co KG

In 2017, the former Kommunalkredit Beteiligungs- und Immobilien GmbH (KBI) was merged into Kommunalkredit Austria AG. Since the merger, all participations of the former KBI have been directly held by Kommunalkredit Austria AG. KBI's real estate assets, representing the office location of the bank, were transferred to a special-purpose vehicle (Kommunalkredit TLI Immobilien GmbH & Co KG), which is fully controlled by Kommunalkredit.

Kommunalleasing GmbH

Kommunalleasing GmbH is a 50% joint venture with BAWAG P.S.K.; the company finances a portfolio of EUR 81.1m in the municipal leasing sector, covering around 70 projects. It has not been engaged in any new transactions since August 2008, following changes in tax legislation for municipalities.

Kommunalkredit Vermögensverwaltungs-GmbH in liquidation

The company, which was no longer operational in recent years, was liquidated at the end of September 2017.

RISK REPORTING

For details on the Kommunalkredit Group's risk management, please refer to Note 68 of the Consolidated Financial Statements of the Kommunalkredit Group.

INTERNAL CONTROL SYSTEM (ICS)

Introduction

The objective of the internal control system (ICS) is to support the management in the implementation of effective and continuously improving internal controls, especially in terms of compliance with the relevant legal provisions, the regularity of accounting practices, the reliability of financial reporting and the effectiveness and efficiency of operational processes. The ICS is intended, on the one hand, to ensure compliance with guidelines and regulations and, on the other hand, to create the prerequisites for specific control measures to be applied in key accounting and financial reporting processes. Its primary goals include the correct and transparent disclosure of the assets, the financial position and the income of the company, as well as ensuring compliance with regulatory requirements.

The internal control system of Kommunalkredit comprises five interrelated components: control environment, risk assessment, control measures, information and communication, and supervision.

Control environment

The corporate culture as the overall framework for all management and staff activities represents the fundamental aspect of the control environment. Central organisational principles concern the avoidance of conflicts of interest through a strict segregation of front-office and back-office operations, the transparent documentation of core processes and control steps, as well as the consistent implementation of the four-eyes principle. Furthermore, areas of responsibility and the scope of action at top management level are defined and/or limited by the Supervisory Board committees with different functions and the rules of procedure for the Executive Board.

The internal audit unit independently audits all departments for compliance with the internal rules on a regular basis. The head of the internal audit unit and the compliance officer report directly to the Executive Board and the Supervisory Board.

Risk assessment

Kommunalkredit’s risk management is aimed at discovering all identifiable risks and, if necessary, initiating defensive and preventive measures through optimised processes. The risk management system comprises all processes serving to identify, analyse and assess risks. Risks are assessed and monitored by the management. Special attention is paid to risks regarded as material. The internal control measures taken by the units in charge are evaluated on a regular basis.

Control measures

Kommunalkredit has a regulatory system which defines the structures, processes, functions and roles within the company as well as the related control activities. It provides explicit instructions on how to deal with and/or enforce standard operating procedures or guidelines.

This also applies to information processing, the documentation of information sent and received, as well as the avoidance of transaction errors.

All control measures are implemented to ensure that potential errors or non-compliances in financial reporting are prevented and/or discovered and corrected.

IT security control measures are an essential component of the internal control system. The separation of sensitive activities is supported through a restrictive policy of granting IT user authorisations; compliance with the four-eyes principle is strictly enforced.

Information and communication

The individual units of Kommunalkredit and, in particular, its risk controlling and/or accounting units, submit regular reports, including monthly and quarterly results, to the Executive Board, which in turn reports regularly to the Supervisory Board. The head of the internal audit unit and the compliance officer also report directly to the Supervisory Board. Furthermore, the risk managers of the credit risk management and risk controlling units report to the Risk Committee of the Supervisory Board.

Comprehensive reports are submitted to the Supervisory Board and its committees on a regular basis. The flow of information comprises the financial statements (balance sheet and income statement, budget and capital budget, deviations of actual figures from target figures, including comments on significant developments) of the company, comprehensive quarterly risk reports, as well as liquidity risk analyses by the treasury department and analyses of the activities of the market units. The shareholders, investors and market partners as well as the public are informed through the mid-year financial report and the annual financial report. Information is also communicated in the form of ad-hoc disclosures, as required by law.

Supervision

Financial statements to be published are subject to a final review, to be coordinated with the external auditor, and explicitly released by senior accounting staff and the Executive Board prior to their submission to the Audit Committee of the Supervisory Board.

By monitoring compliance with all rules, Kommunalkredit hopes to achieve a maximum level of security for all operational procedures and processes and ensure conformity with all group-wide and legal standards. If risks and weaknesses in the control system are detected, remedial and defensive measures are immediately established and implementation of the follow-up steps is monitored.

To ensure compliance with rules and guidelines throughout the bank, regular audits are performed in accordance with the annual audit plan drawn up by the internal audit unit.

SUSTAINABILITY

Sustainability firmly rooted in Kommunalkredit's business model

Kommunalkredit contributes to the sustainable success of infrastructure projects that improve the quality of people's lives and sustainability is firmly rooted in Kommunalkredit's business model.

An environmental management system according to the EMAS Regulation was established within Kommunalkredit already in 1997. Over the years, it has been developed into an integrated sustainability management system. The principles of sustainability are firmly embedded in Kommunalkredit's day-to-day activities and reflected in a broad range of measures. The importance attributed to a sustainable business model is also expressed in the issuance of the first Austrian social covered bond in 2017.

Kommunalkredit Public Consulting (KPC), a subsidiary of Kommunalkredit, contributes to the sustainable implementation of national and international environmental and climate protection projects. On the one hand, KPC develops and manages support programmes in the environment and energy sectors and contributes to the fight against global warming through Climate Austria, a voluntary carbon compensation programme. On the other hand, KPC supports the development and dissemination of environmental and technological standards through a range of consulting projects (e.g. establishment of credit lines for energy efficiency projects in Russia and the Western Balkan countries).

Sustainability ratings

Sustainability rating agencies have recognised and rewarded Kommunalkredit's commitment to its sustainability management system and its willingness to continuously improve its sustainability performance: In its most recent audit in 2016, Oekom research rated Kommunalkredit as a "PRIME company". The investment research unit of imug (Beratungsgesellschaft für sozial-ökologische Innovationen) recently confirmed its rating of "very positive" for Kommunalkredit's covered bonds. In 2017, Kommunalkredit was awarded "Qualified" status in the sustainability rating of rfu Mag. Reinhard Friesenbichler Unternehmensberatung, an Austrian company specialising in sustainable investment and sustainability analyses.

Ecological and social issues

A mindful use of resources – ranging from waste sorting and waste avoidance to recto/verso printing to ecologically minded business travel planning – is everyday practice at Kommunalkredit. Energy efficiency and the use of renewable resources, e.g. through a pellet-fired heating system in Kommunalkredit's office building and the use of green electricity as well as continuous optimisation of the IT infrastructure with regard to its energy consumption, is another priority. In addition, KPC offsets the CO_2 emissions caused by business travel via www.climateaustria.at.

Within the framework of the ongoing stakeholder dialogue, Kommunalkredit and KPC carried on with a number of cooperation projects in 2017, such as the series of events on “The Courage to be Sustainable” organised by the Austrian Environment Agency. Other cooperating partners include the Austrian Water and Waste Management Association and IG Lebenszyklus Bau, an organisation promoting the life-cycle approach in building construction, as well as the Austrian Society for Environment and Technology.

Internally, the Sustainability Team is a point of contact and a platform for the discussion of all topics and concerns relating to sustainability at the workplace and beyond. These include compliance with EMAS guidelines, a newsletter and information events, sustainability-related film viewings, the book and video lending library, and the sustainability award for private commitment.

Kommunalkredit’s externally audited Sustainability Report for the business year 2016 was published in accordance with the GRI G4 standards on sustainability reporting. The Sustainability Report qualifies as an EMAS environmental declaration and can be downloaded at www.kommunalkredit.at. The Sustainability Report for 2017 will be available from June 2018.

COMPLIANCE AND MONEY LAUNDERING

The Standard Compliance Code of the Austrian banking sector (SCC) signed by Kommunalkredit specifies requirements of fairness and mutual confidence in the relations of banks with their customers that partly go beyond the provisions of the law.

Pursuant to the provisions of the law and the SCC, Kommunalkredit adopted an internal compliance code and introduced a compliance organisation headed by a compliance officer who reports to the Executive Board. In line with the SCC and the relevant legal provisions, the compliance code is primarily aimed at ensuring compliance with the relevant provisions of the Securities Supervision Act and the provisions on market abuse, especially through measures to prevent the abuse of inside information or market manipulation.

In addition, the compliance organisation of Kommunalkredit is responsible for taking the necessary measures to prevent any violation of legal provisions or internal policies that might jeopardise the reputation of the company. It also ensures that the compliance code is kept up to date and observed throughout the Group. The compliance officer of Kommunalkredit acts as a point of contact for all staff members, informing them regularly about the rules and regulations in effect.

In his capacity as anti-money-laundering officer, the compliance officer is also responsible for ensuring compliance with the provisions of the Financial Markets Money-Laundering Act.

OUTLOOK

The European Commission expects GDP growth in the euro zone to remain almost unchanged at 2.3% in 2018 (compared to 2.4% in 2017). [13] It projects a growth rate of 2.3% for Germany (2.2% in 2017) and 1.7% for France (1.6% in 2017). Forecasts for the UK are somewhat muted due to Brexit, with a growth rate of 1.3% (down from 1.5% in 2017).

[13] European Commission, The autumn 2017 forecast.

These figures reflect a stable trend for the European economy, with balanced risks to the growth outlook. External risks relate to an overshooting of the euro exchange rate, geopolitical tensions, trade protectionism, vulnerability of emerging markets to global monetary policy tightening, adverse implications of the looming Brexit as well as the rebalancing of crude oil markets. Especially in the euro zone, however, economic growth momentum continues to be robust and broad-based, driven by private consumption and business investment. Furthermore, growth is supported by steadily rising income and profits as well as expanded lending spurred by favorable financing conditions. Additionally, euro zone exports benefit from stronger foreign demand which partially offsets the effect of the euro appreciation.

A major change of the interest rate landscape is not foreseen in the short term and rates are expected to remain at low levels throughout 2018, with an increasing trend anticipated in the medium term. In December 2017, the European Central Bank (ECB) signalled its intention to maintain its expansionary monetary policy for the euro zone. It will reduce its bond purchases by half to EUR 30bn per month, but continue the programme at least until September 2018.[14] The Bank of England announced that its interest-rate policy will depend largely on the outcome of the Brexit negotiations.[15] The Fed intends to continue its policy of step-by-step interest rate hikes and has announced three upward adjustments each for 2018 and 2019.

In view of the above, conditions for the European infrastructure market are expected to be largely unchanged in 2018. After the steep rise in the previous year, Kommunalkredit expects demand for European infrastructure assets to remain high in 2018. The bank foresees numerous transactions in markets such as Germany, France, Spain, the UK and Scandinavia.

The progress achieved in the business year 2017 provides the bank with an excellent foundation for further business growth in 2018. The major objectives for 2017 were met or exceeded. New business volume contracted amounted to EUR 635.2m. The bank distributed a total volume of EUR 373.2m to institutional investors and banks, including EUR 194.2m from new business and EUR 179.0m from its historic portfolio. The majority of this was placed with asset managers, insurance companies and pension funds. The successful placement with such a variety of leading international investors from different market segments is a clear recognition of the bank's strengthened strategic position combined with an expanded geographic scope as well as project type, especially in the transportation sector. In parallel, the deposit base of the bank could be significantly expanded and with the launch of its online retail platform KOMMUNALKREDIT INVEST, the bank now also operates in the retail market for the first time. The progress on the business generation side goes hand in hand with an increase in efficiency of internal processes, which will lead to a reduction of the cost base in 2018.

Kommunalkredit has started the new business year with well-defined strategic and operative parameters. A dynamic project pipeline promises a continuation of a successful year in business origination and distribution. With a rising operating result and a continued decline in extraordinary income, Kommunalkredit expects its annual result for 2018 to be above the previous year's level. The evolution of the operating structure will depend on the outcome of the tender by KA Finanz AG for services currently provided by Kommunalkredit Austria AG. The bank intends to submit an offer for the continuation of such services. A decision by KA Finanz AG is expected by midyear 2018. Should the bank not be awarded with a continuing contract, the service contract with KA Finanz AG will expire in the first half of 2019. In such case the operative capacity will be adjusted during a contractually existing transition period of 12 months. In the medium term the bank targets a cost income ratio below 50%.

[14] ECB, 14 September 2017.
[15] Bank of England, 2 November 2017.

As of 1 January 2018, the new IFRS 9 accounting standard introducing new rules on the recognition and valuation of financial instruments (loans, securities etc.) has come into effect. Kommunalkredit applies the new rules according to the standard; first adoption of IFRS 9 is expected to result in an increase in IFRS equity by approx. EUR 10m to around EUR 294m compared to 31 December 2017.

Following a positive year 2017, Kommunalkredit Austria AG had a strong start into 2018 and is looking confidently forward to the opportunities and positive challenges of the current business year 2018.

Vienna, 5 March 2018

The Executive Board of
Kommunalkredit Austria AG

Alois Steinbichler	**Jörn Engelmann**	**Karl-Bernd Fislage**	**Wolfgang Meister**
Chief Executive Offer	Member of the Executive Board	Member of the Executive Board	Member of the Executive Board

REPORT OF THE SUPERVISORY BOARD TO THE SHAREHOLDERS' MEETING

The Supervisory Board of Kommunalkredit Austria AG (Kommunalkredit) submits its report on the business year 2017 to the Shareholders' Meeting.

The Supervisory Board comprises four capital representatives, two independent representatives and three employee representatives. As in the previous year, Patrick Bettscheider, delegated by Gesona Beteiligungsverwaltung GmbH, holds the position of Chairman of the Supervisory Board. The three other capital representatives, as in the previous year, are Christopher Guth, Deputy Chairman of the Supervisory Board and delegated by Attestor Capital, Katharina Gehra, Chief Operating Officer of Interritus Limited and Managing Director of Gesona Beteilgungsverwaltung GmbH, and Friedrich Andreae, Managing Director of Gesona Beteiligungsverwaltung GmbH. Jürgen Meisch, Managing Director of Achalm Capital GmbH, continues to exercise his mandate as an independent member of the Supervisory Board. Werner Muhm's mandate expired on 10 March 2017. Subsequently, Martin Rey, Managing Director of Maroban GmbH, was newly appointed to the Supervisory Board on 24 July 2017. The Supervisory Board members delegated by the Staff Council are Patrick Höller and Renate Schneider, as well as Franz Hofer, who resigned from the Supervisory Board on 6 November 2017. As successor to Franz Hofer, Paul Matousek was delegated to the Supervisory Board by the Staff Council as of 6 November 2017. The Supervisory Board wishes to thank all former members who resigned in the course of 2017 for their trust and cooperation.

As of 1 February 2016, Karl-Bernd Fislage was appointed Member the Executive Board responsible for Banking & Markets. At the time of reporting, the Executive Board consists of Chairman Alois Steinbichler (Chief Executive Officer), Wolfgang Meister (Chief Operating Officer), Jörn Engelmann (Chief Risk Officer) and Karl-Bernd Fislage (Banking & Markets).

Kommunalkredit looks back on a successful year. The bank has made substantial progress in its efforts to position itself as a strong market participant for infrastructure finance in Europe. Kommunalkredit succeeded in significantly expanding its new business, strengthening its funding base and investing in new strategic initiatives, such as the online retail platform KOMMUNALKREDIT INVEST. Kommunalkredit Public Consulting (KPC), a 90% subsidiary of Kommunalkredit, continues to operate in the field of support programme management.

The Supervisory Board performed its tasks, as defined in the Articles of Association and the Rules of Procedure, within the framework of four ordinary meetings and one constituent meeting. Moreover, the statutory committees (Nomination Committee, Audit Committee, Risk Committee, Remuneration Committee and Credit Committee) held their meetings and performed their tasks. The Rules of Procedure of the Supervisory Board were amended to allow for the exchange of Supervisory Board communication (i.e. circular resolutions, convocation of meetings, distribution of meeting documents/information) by secure electronic means. Moreover, on account of the enlargement of the Executive Board and the reorganisation of business units, the division of tasks and responsibilities among the Executive Board members was newly defined and adopted.

In the course of the meetings of the Supervisory Board and its committees, as well as through regular information obtained orally and in writing, the Supervisory Board was continuously updated on the development of business, the position and performance of the company and its business policy plans. In exercising its tasks conferred upon it by law, the Articles of Association and the Rules of Procedure, the Supervisory Board advised and supervised the Executive Board in the management of the company. In accordance with the fit-and-proper guideline (based on the European Banking Authority Guideline), the members of the Boards of the bank underwent comprehensive fit-and-proper training covering regulatory changes and/or innovations in the autumn of 2017.

These Financial Statements and the Management Report were audited by PwC Wirtschaftsprüfung GmbH Wirtschaftsprüfungs- und Steuerberatungsgesellschaft, Vienna. The audit did not result in any findings. Given that all legal requirements were complied with by the bank and the annual financial statements present a true and fair view of the assets and the financial position of the company as at 31 December 2017, the auditors issued an unqualified audit opinion. Having examined the financial statements, the Supervisory Board endorsed the result of the audit and approved the 2017 Financial Statements at its meeting on 6 March 2018, which were thus formally adopted. Moreover, the Consolidated Financial Statements as at 31 December 2017, including the Management Report, were examined and taken note of by the Supervisory Board.

Vienna, 5 March 2018

The Supervisory Board

Patrick Bettscheider
Chairman

CONSOLIDATED FINANCIAL STATEMENTS OF THE KOMMUNALKREDIT GROUP, VIENNA, FOR THE BUSINESS YEAR 2017

I. CONSOLIDATED BALANCE SHEET ACCORDING TO IFRS

Assets **in EUR 1,000**	**Note**	**31/12/2017**	**31/12/2016**
Cash and balances with central banks	(25)	318,109.1	310,457.4
Loans and advances to banks	(26)	140,197.5	101,865.4
Loans and advances to customers	(27)	2,091,879.7	2,138,929.0
Assets designated at fair value through profit or loss	(28)	605,731.1	691,616.0
Assets available for sale	(29)	211,564.2	146,950.4
Derivatives	(30)	232,616.8	337,156.4
Investments in associates	(31)	0.0	0.0
Property, plant and equipment	(32)	25,850.3	26,940.9
Intangible assets	(33)	191.4	288.7
Current tax assets	(35)	476.5	3,249.1
Deferred tax assets	(35)	27,243.6	15,841.2
Other assets	(36)	9,370.4	17,510.6
Assets		**3,663,230.7**	**3,790,805.0**

Liabilities and equity **in EUR 1,000**	**Note**	**31/12/2017**	**31/12/2016**
Amounts owed to banks	(37)	532,838.2	795,027.9
Amounts owed to customers	(38)	1,038,002.0	552,093.0
Derivatives	(39)	244,709.4	263,347.5
Securitised liabilities	(40)	1,468,582.1	1,779,165.4
Subordinated liabilities	(41)	68,922.1	69,846.8
Provisions	(42)	7,594.2	7,819.6
Current tax liabilities	(43)	599.8	1,695.3
Other liabilities	(44)	18,857.9	25,030.5
Equity	(45)	283,125.0	296,779.0
of which subscribed capital		*159,491.3*	*159,491.3*
of which statutory reserves		*14,241.5*	*13,298.2*
of which available-for-sale reserve		*892.4*	*1,290.9*
of which other reserves (incl. consolidated net profit)		*108,339.7*	*122,544.2*
of which non-controlling interests		*160.1*	*154.5*
Liabilities and equity		**3,663,230.7**	**3,790,805.0**

II. CONSOLIDATED INCOME STATEMENT ACCORDING TO IFRS

Income Statement in EUR 1,000	Note	1/1-31/12/2017	1/1-31/12/2016
Net interest income	(46)	35,217.8	36,521.7
Interest and similar income		*157,134.9*	*172,112.2*
Interest and similar expenses		*-121,917.1*	*-135,590.5*
Net provisioning for impairment losses	(47)	-300,4	64,6
Net fee and commission income	(48)	17,258.3	16,789.8
Fee and commission income		*18,135.7*	*17,312.4*
Fee and commission expenses		*877,4*	*-522.6*
Income from other investments		158.1	77.9
Income from investments in associates		0.0	-2,322.4
Net trading and valuation result	(49)	3,066.4	36,231.5
General administrative expenses	(50)	-58,648.3	-49,330.0
Contributions to the Bank Resolution Fund	(51)	-949.5	-2,508.5
Other operating result	(52)	11,248.7	-115.9
Other operating income		*12,531,6*	*11,542.0*
Other operating expenses		*-1,282,8*	*-11,657.9*
Consolidated profit for the year before tax		**7,051.3**	**35,408.7**
Taxes on income	(53)	11,003.4	13,546.7
Consolidated net profit		**18,054.7**	**48,955.3**

of which attributable to owners	*18,012.7*	*48,905.3*
of which attributable to non-controlling interests	*42.0*	*50.0*

III. CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Comprehensive income in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
Consolidated profit for the year	**18,054.7**	**48,955.3**
Items to be recycled to the Income Statement	**-398.5**	**-287.2**
Change in available-for-sale reserve	**-398.5**	**-287.2**
Valuation of available-for-sale portfolio	*-531.3*	*-383.0*
Deferred tax on available-for-sale reserve	*132.8*	*95.7*
Items not to be recycled to the Income Statement	**744.6**	**-98.7**
Change in actuarial result	**744.6**	**-98.7**
Actuarial result from pension provisions	*992,8*	*-131,6*
Deferred tax on actuarial result from pension provisions	*-248.2*	*32.9*
Comprehensive income	**18,400.9**	**48,569.4**

of which attributable to owners	*18,340.3*	*48,519.3*
of which attributable to non-controlling interests	*60.6*	*50.0*

IV. CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Equity according to IFRS developed as follows in 2017 and 2016:

Development of equity 2017 in EUR 1,000	Subscribed capital	Statutory reserves[1]	Retained earnings and other reserves	Profit for the year (attributable to owners)	Available-for-sale-reserve[2]	Actuarial gains/ losses IAS 19	Equity excl. non-controlling interests	Non-controlling interests	Equity
as at 1/1/2017	**159,491.3**	**13,298.2**	**73,441,3**	**48,905.3**	**1,290.9**	**197.6**	**296,624.6**	**154.5**	**296,779.0**
Profit for the year	**0.0**	**0.0**	**0.0**	**18,012.7**	**0.0**	**0.0**	**18,012.7**	**42.0**	**18,054.7**
Change in AFS reserve	0.0	0.0	0.0	0.0	-398.5	0.0	**-398.5**	0.0	**-398.5**
Valuation of AFS portfolio	*0.0*	*0.0*	*0.0*	*0.0*	*-398.5*	*0.0*	***-398.5***	*0.0*	***-398.5***
Recycling of AFS reserve	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	***0.0***	*0.0*	***0.0***
Change in actuarial gains/losses	0.0	0.0	0.0	0.0	0.0	726.1	**726.1**	18.6	**744.6**
Comprehensive income	**0.0**	**0.0**	**0.0**	**18,012.7**	**-398.5**	**726.1**	**18,340.3**	**60.6**	**18,400.9**
Distributions	0.0	0.0	-32,000.0	0.0	0.0	0.0	**-32,000.0**	-54.9	**-32,054.9**
Transfers	0.0	943.3	47,962.0	-48,905.3	0.0	0.0	**0.0**	0.0	**0.0**
as at 31/12/2017	**159,491.3**	**14,241.5**	**89,403.3**	**18,012.7**	**892.4**	**923.7**	**282,964.8**	**160.1**	**283,125.0**

[1] Statutory reserves include retained earnings in the amount of TEUR 4,241.5 and other statutory reserves of the parent pursuant to § 57 (5) of the Austrian Banking Act in the amount of TEUR 10,000.0.

[2] The available-for-sale reserve comprises deferred taxes of TEUR -297.5 as at 31 December 2017.

Development of equity 2016 in EUR 1,000	Subscribed capital	Statutory reserves[1]	Retained earnings and other reserves	Profit for the year (attributable to owners)	Available-for-sale-reserve[2]	Actuarial gains/ losses IAS 19	Equity excl. non-controlling interests	Non-controlling interests	Equity
as at 01/01/2016	**159,491.3**	**10,508.7**	**78,690.4**	**5,540.4**	**1,578.1**	**296.4**	**256,105.2**	**158.6**	**256,263.8**
Profit for the year	**0.0**	**0.0**	**0.0**	**48,905.3**	**0.0**	**0.0**	**48,905.3**	**50.0**	**48,955.3**
Change in AFS reserve	0.0	0.0	0.0	0.0	-287.2	0.0	**-287.2**	0.0	**-287.2**
Valuation of AFS portfolio	*0.0*	*0.0*	*0.0*	*0.0*	*-287.2*	*0.0*	***-287.2***	*0.0*	***-287.2***
Recycling of AFS reserve	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	***0.0***	*0.0*	***0.0***
Change in actuarial gains/losses	0.0	0.0	0.0	0.0	0.0	-98.7	**-98.7**	0.0	**-98.7**
Comprehensive income	**0.0**	**0.0**	**0.0**	**48,905.3**	**-287.2**	**-98.7**	**48,519.3**	**50.0**	**48,569.4**
Distributions	0.0	0.0	-8,000.0	0.0	0.0	0.0	**-8,000.0**	-54.2	**-8,054.2**
Transfers	0.0	2,789.5	2,751.0	-5,540.4	0.0	0.0	**0.0**	0.0	**0.0**
as at 31/12/2016	**159,491.3**	**13,298.2**	**73,441.3**	**48,905.3**	**1,290.9**	**197.6**	**296,624.6**	**154.5**	**296,779.0**

[1] Statutory reserves include retained earnings in the amount of TEUR 3,298.2 and other statutory reserves of the parent pursuant to § 57 (5) of the Austrian Banking Act in the amount of TEUR 10,000.0.

[2] The available-for-sale reserve comprises deferred taxes of TEUR -430.3 as at 31 December 2016.

For details on equity, see Note 45.

V. CONSOLIDATED STATEMENT OF CASH FLOWS

The Consolidated Statement of Cash Flows shows the current state and the development of the Kommunalkredit Group's cash and cash equivalents. Strictly interpreted, cash and cash flow equivalents include cash in hand and balance with central banks.

Consolidated statement of cash flows in EUR 1,000	1/1- 31/12/2017	1/1- 31/12/2016
Consolidated profit for the year after tax	**18,054.7**	**48,955.3**
Non-cash items included in the profit for the year and reconciliation to cash flow from operating activities		
Depreciation and amortisation of property, plant and equipment and intangible assets	1,780.1	2,017.8
Appropriation to/release of provisions	341.5	279.4
Non-realised gains/losses from exchange rate fluctuations	-9.4	5.5
Gains/losses from the valuation of financial assets and gains from the buyback of own issues	-3,057.0	-36,236.9
Income tax deferrals	-9,840.7	-19,489.8
Profit participations in companies valued according to the equity method	0.0	2,322.4
Non-cash deferrals/accruals and other adjustments	-1,831.1	-1,094.6
Sub-total	**5,438.0**	**-3,240.9**
Change in assets and liabilities from operating activities after correction for non-cash items		
Loans and advances to banks	-38,323.7	139,074.7
Loans and advances to customers	47,444.0	203,922.8
Assets available for sale and fair-value option	-12,542.1	54,077.8
Derivatives	155,800.9	73,472.3
Other assets from operating activities	8,140.1	-9,708.4
Amounts owed to banks	-260,752.2	331,046.2
Amounts owed to customers	484,294.3	164,157.2
Securitised liabilities	-342,313.1	-718,751.1
Other liabilities from operating activities	-6,046.9	6,524.7
Cash flow from operating activities	**41,139.3**	**240,575.5**
Proceeds from the sale/redemption of		
Financial assets	0.0	0.0
Property, plant and equipment and intangible assets	0.0	2.0
Payments for the acquisition of		
Financial assets	0.0	0.0
Property, plant and equipment and intangible assets	-592.1	-1,208.3
Cash flow from investing activities	**-592.1**	**-1,206.3**
Cash inflow from capital increases/cash outflow from capital reductions	0.0	0.0
Dividend payments attributable to the owners of the parent	-32,000.0	-8,000.0
Dividend payments attributable to non-controlling interests	-54.9	-54.2
Change in funds from other financing activities (subordinated capital)	-840.6	-550.8
Cash flow from financing activities	**-32,895.5**	**-8,605.0**
Cash and cash equivalents at the of the previous period	**310,457.4**	**79,693.3**
Cash flow from operating activities	41,139.3	240,575.5
Cash flow from investing activities	-592.1	-1,206.3
Cash flow from financing activities	-32,895.5	-8,605.0
Cash and cash equivalents at the end of the period	**318,109.1**	**310,457.4**

of which cash flows contained in cash flow from operating activities:		
Interest received	148,522.5	149,862.8
Interest paid	-111,464.2	-112,251.9
Taxes on income paid	1,376.2	3,631.6
Dividends received	161.0	77.9

Development of subordinated liabilities carried on the balance sheet	**2017**	**2016**
as at 1/1	69,846.8	73,848.2
Changes in cash items	-840.6	-550.8
Changes in non-cash items (primarily from hedge accounting)	-84.1	-3,450.6
as at 31/12	68,922.1	69,846.8

NOTES TO THE FINANCIAL STATEMENTS OF THE KOMMUNALKREDIT GROUP, VIENNA, FOR THE BUSINESS YEAR 2017

GENERAL PRINCIPLES

1. GENERAL INFORMATIONEN

Kommunalkredit Austria AG (Kommunalkredit), with its registered office in Vienna, Türkenstrasse 9, is positioned as a specialist bank in the fast growing market for infrastructure finance. It acts as a link between infrastructure developers, such as municipalities, public-sector enterprises or private project sponsors, on the one hand, and institutional investors, such as insurance companies and pension funds, on the other hand. It is registered with the Commercial Court of Vienna under Companies Register number 439528s.

Kommunalkredit was established on 26 September 2015 through the demerger for new incorporation of the former Kommunalkredit. The entire business operation of the former Kommunalkredit (including all its subsidiaries) was transferred to a newly incorporated company (Kommunalkredit) by way of a proportionate demerger for new incorporation. The part of the former Kommunalkredit remaining after the demerger, which comprised high-quality assets as well as positive equity and debt instruments issued for funding, was merged into KA Finanz AG (KF).

Gesona Beteiligungsverwaltung GmbH (Gesona) owns 99.78% of Kommunalkredit. The remaining 0.22% is held by the Association of Austrian Municipalities. Gesona is a holding company through which Interritus Limited (Interritus) and Trinity Investments Designated Activity Company (Trinity) – via Satere Beteiligungsverwaltungs GmbH (Satere) – hold their participations in Kommunalkredit; Interritus and Trinity, respectively, hold 55% and 45% of Satere, which in turn holds 100% of Gesona.

The consolidated financial statements of Kommunalkredit, based on the International Financial Reporting Standards (IFRS) applicable in the European Union (EU), are prepared pursuant to § 59a of the Austrian Banking Act (*Bankwesengesetz – BWG*) in conjunction with § 245a of the Austrian Company Code (*Unternehmensgesetzbuch – UGB*). These financial statements meet the requirements of § 59a of the Austrian Banking Act. As an issuer of exchange-listed securities, Kommunalkredit publishes a Group Management Report pursuant to § 124 (1) of the Austrian Stock Exchange Act as part of this Annual Financial Report.

2. STANDARDS AND INTERPRETATIONS APPLIED

The consolidated financial statements of Kommunalkredit were prepared on the basis of the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS) adopted and published by the International Accounting Standards Board (IASB) and to be applied on a mandatory basis as of 31 December 2017, as adopted by the European Union (EU), as well as the interpretations by the IFRS Interpretations Committee (IFRIC and SIC).

New International Financial Reporting Standards applicable to future annual periods

An overview of the new IFRS applicable to future annual periods, already adopted or expected to be adopted by the EU and transposed into European law, is given below. The order of presentation is based on the relevance of the new standards for Kommunalkredit.

IFRS 9 (Financial Instruments)

IFRS 9 “Financial Instruments”, published in July 2014 and applicable to annual periods beginning on or after 1 January 2018, fully replaces IAS 39 “Financial Instruments: Recognition and Measurement”. IFRS 9 comprises three parts:

1. Classification and measurement of financial instruments
2. Risk provisioning on the basis of the expected-credit-loss model
3. Hedge accounting

The new provisions will be applied retroactively by Kommunalkredit from 1 January 2018 with the practical expedients permitted under the standard. All portfolios are to be reclassified at the time of first adoption of IFRS 9 of 1 January 2018, irrespective of their current treatment. The carrying amounts are adjusted directly in equity. Comparative values for the year 2017 are not restated. Instead, the one-off effect of the first-time adoption of IFRS 9 in equity will be reflected in the opening balance sheet as of 1 January 2018.

Kommunalkredit largely completed the operational implementation of IFRS 9 in the course of 2017 and will apply the new rules according to the standard.

First adoption of IFRS 9 is expected to result in an increase in equity by approx. EUR 10m, comprising
- EUR +13.5m resulting from the adjustment of the carrying amounts within the framework of the reclassification of assets and the related deferred taxes
- EUR -3.5m resulting from the increase in risk provisions based on the application of the expected-credit-loss model

The material implications are described in detail below:

Classification and measurement

IFRS 9 provides for all financial assets to be measured either at amortised cost or at fair value, depending on the business model and the terms and conditions of the contractual cash flows. Accounting at fair value is possible either through equity (Other result) or through profit or loss.

Assets held within the framework of a business model aimed at generating contractual cash flows which are solely payments of principal and interest (SPPI criterion) on the capital outstanding, are to be accounted at amortised cost in subsequent periods. If the financial assets exclusively generate cash flows meeting the SPPI criterion and are held within the framework of a business model intended to generate income both through contractual cash flows and through sales, these assets are accounted for at fair value through equity. All other financial assets have to be accounted for at fair value through profit or loss.

Moreover, companies can elect to measure financial instruments at fair value at the time of purchase or origination, if incongruencies resulting from different measurement methods can thus be eliminated or reduced (fair value option). Kommunalkredit does not elect to apply the fair value option as of 1 January 2008.

Equity instruments not held for trading can be measured at fair value through equity; Kommunalkredit will elect to apply this option.

The analyses performed by Kommunalkredit within the framework of its implementation of IFRS 9 led to the conclusion that the financial assets held as of 1 January 2018 (mainly loans and securities) meet the SPPI criterion and therefore have to be classified on the basis of the relevant business model. This classification results in the following changes in the accounting and measurement category, as compared to IAS 39:

- Loans in an IAS 39 carrying amount of EUR 547.0m as at 31 December 2017 will be allocated to the “hold to sell portfolio”, as sales cannot be precluded. According to IAS 39, this portfolio was accounted for partly at amortised cost (EUR 191.3m) and partly at fair value through profit or loss (EUR 355.7m).
- Loans in an IAS 39 carrying amount of EUR 250.1m are allocated to the “hold to collect portfolio”, as these positions are to be held in the long term, whereas according to IAS 39 they were accounted for at fair value through profit or loss.
- Infrastructure finance positions in a carrying amount of EUR 135.8m as at 31 December 2017, for which the possibility of placement with institutional investors is taken into consideration, are allocated to the “hold to collect and sell portfolio”. According to IAS 39, these loans were accounted for at amortised cost.
- Securities portfolios which, according to IAS 39, were allocated to the available-for-sale category, are to be allocated to the “hold to collect” business model. As at 31 December 2017, the carrying amount of the portfolio is approx. EUR 208.7m.

Assets held with the intention to trade or to generate short-term gains are allocated to the “hold to sell” business model; for the time being, this business model is of little relevance to Kommunalkredit. As at 1 January 2018, there are no portfolios allocated to this business model.

Primarily, the classification and measurement of financial liabilities within the framework of IFRS 9 remains unchanged compared to the rules applicable under IAS 39. The only exception are changes in the fair value of financial liabilities in the fair value option resulting from changes in the company’s own credit risk; Kommunalkredit is not concerned by this change, as it does not carry any financial liabilities in its fair value portfolio, neither according to IAS 39 nor according to IFRS 9.

Risk provisioning on the basis of the expected-credit-loss model

The new impairment model of IFRS 9 requires the recognition of impairments on the basis of expected credit losses instead of credit losses incurred, as was the case under IAS 39. This concerns financial instruments measured at amortised cost or at fair value through equity.

The risk provision is to be recognised either in the amount of the expected 12-month credit loss (stage 1) or the full lifetime expected credit loss (stage 2), depending on whether the risk of default has increased significantly since the initial recognition of the asset. To assess whether the risk of default has increased significantly (stage transfer), Kommunalkredit considers quantitative and qualitative factors. These comprise, in particular:

- Absolute amount of the credit risk
- Relative change in credit risk based on the rating
- Changes in internal price indicators, with terms and conditions remaining the same
- Possible significant change in contractual conditions if the financial instrument were newly issued
- Changes in external market indicators of a comparable financial instrument

Given the high asset quality of Kommunalkredit's current portfolio (89.4% of the portfolio rated investment grade as of 31 December 2017, 46.6% of which in the "AAA"/"AA" range), less than 1% of the portfolio will presumably have to be allocated to stage 2.

The calculation of the expected credit loss is probability-weighted and considers all expected cash outflows and inflows as well as the maximum contractual term during which Kommunalkredit is exposed to a risk of default. The input parameters for the calculation of the expected credit losses, such as exposure at default (EAD), probability of default (PD) and loss given default (LGD) are derived from a combination of internal and external data in accordance with the rules.

Forecasts of future events to be included in establishing the input parameters are based on a macroeconomic model considering GDP growth, the rate of unemployment and changes in various indices. When deriving macroeconomic scenarios as a basis for the probability-weighted calculation of expected credit losses, the specific features of Kommunalkredit's portfolios are taken into consideration; these scenarios are subject to periodic validation.

The change-over to IFRS 9 will presumably result in an increase in the amount of impairments shown at the beginning of 2018, as compared to the year-end amount of risk provisions according to IAS 39 (including provisions for off-balance-sheet exposures according to IAS 37) by approx. EUR 3.5m.

Hedge accounting

Hedge accounting under IFRS 9 will be aligned more closely with a company's economic risk management in order to reflect its risk management strategy more clearly in its financial statements. Kommunalkredit will continue all its current hedging relationships and apply the IFRS 9 hedge accounting rules to them. No material impact is expected.

IFRS 15 (Revenue from Contracts with Customers)

"Revenue from Contracts with Customers" applies to the realisation of revenue and replaces IAS 11 "Construction Contracts", IAS 18 "Revenue", SIC 31 "Revenue – Barter Transactions Involving Advertising Services", IFRIC 13 "Customer Loyalty Programmes", IFRIC 15 "Agreements for the Construction of Real Estate" and IFRIC 18 "Transfer of Assets from Customers". The objective of IFRS 15 is to create principles to be applied by a company when providing useful information to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. According to IFRS 15, revenue is to be recognised when the customer obtains control of the promised goods and services and can derive a benefit from them. The new standard provides for a five-step process for the determination of revenue to be realised. IFRS 15 contains numerous disclosure requirements regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

IFRS 15 is to be applied for annual periods beginning on or after 1 January 2018. The management has analysed the consequences of applying the new standard to the consolidated financial statements and has arrived at the conclusion that there will be no material impact.

IFRS 16 (Leases)

IFRS 16 "Leases" specifies how to recognise, measure, present and disclose leases. The standard provides a single accounting model for the lessee. Lessees are required to recognise assets and liabilities for all leases, unless the lease term is 12 months or less or the underlying asset has a low value. As a practical expedient, lessees have a choice of several options. For accounting purposes, lessors will continue to distinguish between finance leases and operating leases. In this respect, the accounting model according to IFRS 16 does not differ materially from the IAS 17 model.

IFRS 16 is to be applied for annual periods beginning on or after 1 January 2019. Kommunalkredit does not expect a material impact on its future annual statements.

IFRS 4 (Adoption of IFRS 9 together with IFRS 4)

The amendments to IFRS 4 "Insurance Contracts" were published in September 2016 in order to address accounting issues arising from the different dates of first adoption of IFRS 9 "Financial Instruments" and the new standard governing the accounting of insurance contracts (IFRS 17). The amendments to IFRS 4 offer two possibilities: temporary suspension of application of IFRS 9 for insurance companies meeting certain criteria, or the so-called overlay approach. Both approaches are voluntary and may only be applied until 1 January 2021. Kommunalkredit does not expect an impact on its financial statements.

Annual improvements 2014-2016 (IFRS 1, IAS 28)

The "Annual Improvements of IFRS (improvement cycle 2014-2016)" published on 8 December 2016 contain amendments to the following IFRS, which have already been endorsed by the EU but have not been subject to earlier application:

- IFRS 1“First-time Adoption of International Financial Reporting Standards”
  Through this amendment, short-term exemptions for first-time adopters in connection with the transitional rules of IFRS 7, IAS 19 and IFRS 10 were deleted. These transitional rules applied to previous reporting periods, but are no longer applicable.

- IAS 28 “Investments in Associates and Joint Ventures”
  According to IAS 28, venture capital organisations, investment funds, unit trust or similar companies can elect to recognise their investments in associates or joint ventures according to IFRS 9 at fair value through profit or loss. The amendment explicitly clarifies that this election is available at the time of initial recognition and has to be exercised separately for each associate or joint venture.

These amendments apply to annual periods beginning on or after 1 January 2018. They will have no impact on Kommunalkredit’s financial statements.

IFRS 2 (Share-based Payment)

The amendments address individual issues arising in connection with the accounting of cash-settled share-based payment transactions. The most important amendment consists in the inclusion of rules concerning the measurement of the fair value of obligations arising from share-based payments.

These amendments apply to annual periods beginning on or after 1 January 2018. They will have no impact on Kommunalkredit’s financial statements.

IAS 40 (Investment Property)

The amendments serve to clarify the rules regarding transfers of property to, or from, investment property. More specifically, the question is whether a property under construction or development that was previously classified as inventory can be transferred to investment property when there is an evident change in use.

These amendments apply to annual periods beginning on or after 1 January 2018. No material impact on the assets, the financial position and the income of the Group is to be expected.

IFRIC 22 (Foreign Currency Transactions and Advance Consideration)

The interpretation clarifies which exchange rate is to be applied at the time of initial recognition of a foreign currency transaction in the functional currency of a company, if the company pays or receives advance consideration.

IFRIC 22 is to be applied to annual periods beginning on or after 1 January 2018. No material impact on the assets, the financial position and the income of the Group is to be expected.

IFRS 9 (Prepayment Features with Negative Compensation)

The amendments are to allow financial instruments with prepayment options under which a party receives or pays adequate compensation (adequate negative consideration) to qualify for measurement at amortised costs or measurement at fair value through other comprehensive income (FVOCI).

The amendments apply to annual periods beginning on or after 1 January 2019. The impact of the amendments is yet to be analysed.

IAS 28 (Long-term Interests in Associates and Joint Ventures)

This amendment clarifies that IFRS 9 applies to the accounting and measurement of long-term interests that form part of the net investment in an entity accounted for at equity. Therefore, any impairment of these interests is determined according to IFRS 9 rules.

The amendments apply to annual periods beginning on or after 1 January 2019. The impact of the amendments is yet to be analysed.

Annual improvements 2015-2017 (Amendments to and Clarifications of Various IFRS)

The "Annual improvements of IFRS (improvement cycle 2015-2017)" published on 12 December 2017 contain amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23.

- Amendments to IFRS 3 "Business Combinations" and IFRS 11 "Joint Arrangements"
  - If a company, by acquiring additional interests, obtains control of a former joint operation, as defined in IFRS 10, the rules of IFRS 3 on step acquisitions apply and the formerly held interest is to be re-measured according to IFRS 3.42. Moreover, the IASB clarifies that not only the assets and liabilities previously accounted for on a pro-rata basis, but the entire previously held interest in the joint operation is to be re-measured.
  - If a company, by acquiring additional interest, does not obtain control, but merely joint management of a joint operation, the amendments clarify that re-measurement of the previously held interest in the joint operation is not required.

- Amendments to IAS 23 "Borrowing Costs"
  The amendments explicitly clarify that outstanding borrowings made originally to acquire a specific qualified asset, from the point in time when this qualified asset is ready for its intended use or sale, is to be included in the determination of the general borrowing cost ratio for other qualified assets for which no special borrowings were made.

- Amendments to IAS 12 "Income Taxes"
  The amendment aims to clarify the recognition of the tax effect of dividend payments. Accordingly, and in line with the original standard, the income tax consequences of dividend payments are to be treated in the same way as the transaction(s) from which the tax effect originally arose.

The amendments apply to annual periods beginning on or after 1 January 2019. The impact of the amendments is yet to be analysed.

IFRIC 23 (Uncertainty over Income Tax Treatment)

The interpretation contains rules on the recognition and measurement of tax risk positions and thus closes the gaps in the IAS 12 rules on income tax. According to IFRIC 23, complete information of the tax authorities is to be assumed in the assessment of tax risk positions. Moreover, tax-related facts constituting a risk may have an impact on the determination of current and deferred taxes. The published interpretation also contains references to disclosure obligations according to IAS 1.122 and IAS 1.125-1.129 regarding judgments, assumptions and estimates made within the framework of the accounting of tax risk positions. Furthermore, reference is made to rule IAS 12.88 and the duty to disclose any tax-related contingent liabilities and contingent assets.

IFRIC 23 is to be applied to annual periods beginning on or after 1 January 2019. No material impact on the assets, the financial position and the income of the Group is to be expected.

IFRS 17 (Insurance Contracts)

This standard published by the IASB on 18 May 2017 contains rules on the accounting of assets and liabilities resulting from insurance contracts. These rules do not only apply to insurance companies but also to other industries, if the contracts meet the definition of an insurance contract. The term “insurance risk”, for instance, also applies to product and residual value risks.

IFRS 17 provides for three approaches to the presentation of insurance contracts:

- The Building Block Approach (BBA) is the basic model for the presentation of insurance contracts. It applies to all insurance contracts within the scope of IFRS 17, unless one of the following exceptions is applied.
- The Premium Allocation Approach (PAA) is a simplified version of the Building Block Approach applicable to insurance contracts for which measurement according to the PAA does not materially differ from measurement according to the BBA, or which have a short coverage period.
- The Variable Fee Approach (VFA) is yet another version of the Building Blocks Approach for insurance contracts with payments contractually linked to direct participating features.

IFRS 17 is to be applied to annual periods beginning on or after 1 January 2021. No impact on the assets, the financial position and the income of the Group is to be expected.

Amendments to IFRS 10 and IAS 28

The amendments address a conflict between the rules of IAS 28 “Investments in Associates and Joint Ventures” and IFRS 10 “Consolidated Financial Statements”. They clarify that in the case of transactions with associates or joint ventures the extent of gain or loss recognition depends on whether the assets sold or contributed constitute a business as defined in IFRS 3 “Business Combinations”. Entry into force of the amendments has been postponed indefinitely.

The implications of the amendments will still have to be analysed.

Amended standards applicable as of 1 January 2017

IAS 12 (Income Taxes)

The amendments clarify the accounting of deferred tax assets for non-realised losses from debt instruments measured at fair value. In particular, the amendments confirm the following:

- Reduction of the IFRS carrying amount resulting from fair value measurement, while its tax base remains unchanged, always result in a temporary difference, regardless of what the company's intentions for the asset are (sell, hold to maturity).

- The IFRS carrying amount is relevant for the determination of temporary differences, but not for the estimate of the future taxable profit.

- When determining the taxable amount, the realisation of a value exceeding the current IFRS carrying amount is conceivable to the extent that it is probable. If tax law limits the sources of the taxable amount against which deductions can be made when deductible temporary differences are released, these differences can only be taken into account in combination with other deductible temporary differences of the same type in the assessment if and to what extent deferred tax assets are to be recognised. The future taxable amount against which deductible temporary differences can be used is to be determined on the basis of the profit before the reversal of any deductible differences.

IAS 7 (Statements of Cash Flows)

The amendments are intended to improve information provided about the company's financing activities. The amendments require additional disclosures on the development of those borrowed capital items of the balance sheet during the reporting period for which related cash flows were, or future cash flows will be, classified in the statement of cash flows as cash flows from investing activities. Moreover, additional disclosures are required on the development of the balance sheet value of financial assets for which related cash flows are also recognized in cash flows from investing activities.

In particular, disclosures are required on:
- cash-relevant changes arising from changes of financing cash flows
- changes arising from obtaining or losing control of subsidiaries or other businesses
- the effect of changes in foreign exchange rates
- changes arising from changes in fair values, and
- other changes

In addition, sufficient information has to be provided for users of the financial statements to enable them to align the information contained in the reconciliation with the values reported on the balance sheet and in the statement of cash flows.

Annual improvements 2014-2016 (Amendments to IFRS 12)

The annual improvements of IFRS (improvement cycle 2014-2016) published on 8 December 2016 concerning amendments to IFRS 12 “Disclosures on Interests in Other Entities” clarify that the disclosure requirements of IFRS 12 also apply to interests classified according to IFRS 5 as available for sale, except for the summarised financial information according to IFRS 12.B10-B16.

To the extent applicable, the provisions outlined above have been implemented in these financial statements. The amendments to IAS 7 require additional disclosures to be published by the Group. The amendments to IAS 12 as well as the amendments to IFRS 12 have no material impact on the presentation of the assets, the financial position and the income of the Group.

3. SCOPE OF CONSOLIDATION

According to the rules of IFRS 10, the scope of consolidation of the Kommunalkredit Group comprises the following companies, besides Kommunalkredit as the parent, as of 31 December 2017:

Name and registered office	Investment direct	Investment indirect	Share in capital 31/12/2017 in %	Share in capital 31/12/2016 in %	Financial statement disclosures (IFRS) 2017: Last financial statements	Total assets in EUR 1,000	Equity in EUR 1,000	Profit/loss for the year in EUR 1,000
1. Subsidiaries								
Fully consolidated subsidiaries								
Kommunalkredit Beteiligungs- und Immobilien GmbH, Vienna	x		-	100.00%	-	-	-	-
Kommunalkredit Public Consulting GmbH (KPC), Vienna	x		90.00%	90.00%	31/12/2017	7,235.4	1,695.2	420.3
Kommunalkredit KBI Immobilien GmbH	x		100.00%	-	31/12/2017	34.9	34.9	-0.1
Kommunalkredit KBI Immobilien GmbH & Co KG	x		100.00%	-	31/12/2017	32,081.4	32,081.4	0.0
Kommunalkredit TLI Immobilien GmbH & Co KG		x	100.00%	-	31/12/2017	32,057.2	32,019.0	-45.4
2. Associates								
Associates included at equity								
Kommunalleasing GmbH (Kommunalleasing), Vienna	x		50.00%	50.00%	31/12/2017*	81,191.2	5,187.0	126.6

* preliminary unaudited figures

The subsidiaries were included in the scope of full consolidation, while the associate was recognised according to the equity method. The balance sheet date of the consolidated companies is the same as that of the parent.

Kommunalkredit Beteiligungs- und Immobilien GmbH, Vienna, primarily responsible for participation and real estate management within the Kommunalkredit Group, was merged into Kommunalkredit Austria AG by way of the merger agreement of 9 November 2017, effective as of 1 December 2017, date of entry in the Companies Register. Real estate management is now performed by Kommunalkredit KBI Immobilien GmbH, Kommunalkredit KBI Immobilien GmbH & Co KG and Kommunalkredit LTI Immobilien GmbH & Co KG, which were established in the second half of 2017 and do not engage in any other operational activities. The merger and the new establishments had no material impact on the consolidated financial statements of the Kommunalkredit Group.

No material risks or restrictions arise for the Kommunalkredit Group from its subsidiaries. The activities of Kommunalleasing GmbH, included at equity, comprise leasing transactions for Austrian local authorities; the company has not engaged in any new business since 2008. In the reporting year 2016, the book value of the participation in Kommunalleasing GmbH was reduced by TEUR 2,322.4 to TEUR 0.0 and recognised in profit or loss according to IAS 36 rules. No material risks arise for the Kommunalkredit Group from its associates.

ACCOUNTING AND MEASUREMENT PRINCIPLES

4. GENERAL ACCOUNTING AND MEASUREMENT METHODS

The consolidated financial statements of Kommunalkredit were prepared on a going-concern basis. The financial information provided in the consolidated financial statements comprises the data of the parent together with its subsidiaries, presented as one economic entity. The accounting and measurement principles are applied uniformly throughout the Group and continuously for the reporting periods presented.

The financial statements are intended to give a true and fair view of the assets, the financial position and the income of the Kommunalkredit Group according to IFRS rules, as adopted by the EU.

Acquisitions and disposals of all classes of financial assets are recognised on the day of trading.

Income and expenses are accrued/deferred pro-rata-temporis and recognised in profit or loss in the period they count to economically. Interest is recognised as it accrues in net interest income, considering all contractual arrangements made in connection with the financial assets or liabilities. Dividend income is booked on the date on which the legal claim to payment arises.

Fees and commissions for services provided over a certain period of time are recognised over the period of service provision. Fees related to completion of service provision are booked as income at the time of completion. Contingent commissions are recognised when the required performance criteria are met.

The reporting currency of these consolidated financial statements is the euro as the functional currency of all companies of the Group. Unless otherwise indicated, the figures are rounded to the nearest thousand, which may result in rounding differences in the tables.

5. CONSOLIDATION PRINCIPLES

All material subsidiaries controlled by Kommunalkredit, as defined by IFRS 10, are fully consolidated.

The consolidation actions taken include capital consolidation, debt consolidation and the consolidation of expenses and income. The fully consolidated companies all present their annual financial statements as at the Group reporting date.

Within the framework of capital consolidation, all identifiable tangible and intangible assets, liabilities and contingent liabilities of the subsidiary at the time of acquisition are re-measured. The acquisition costs are offset against the pro-rata net assets of the subsidiary at the time of transfer of control. The shares held by the other shareholders are determined on the basis of the assets and liabilities measured at their fair value.

Intra-Group receivables and liabilities as well as expenses and income are eliminated, unless they are immaterial. Intra-Group transactions, balances, and unrealised gains and losses from transactions between Group companies are eliminated, unless they are immaterial.

According to the consolidation rules, joint arrangements (IFRS 11) are accounted for as joint operations and/or joint ventures. Companies over which Kommunalkredit has a material influence and/or joint ventures (investments in associates and joint ventures according to IAS 28) are measured according to the equity method and recognised as investments in associates. According to the equity method, the investments in associates and/or joint ventures are recognised at acquisition cost, plus any post-acquisition changes in the shares held by the Group in the net assets of the associate. The most recent financial statements (including reconciliation to IFRS) of the associate are used as a basis. The pro-rata result (minus dividends paid) is recognised in the Income Statement under “Income from investments in associates”. At every balance sheet date, an impairment test is performed on the basis of financial forecasts. Currently, Kommunalkredit has one associate accounted for according to the equity method (IAS 28).

6. CURRENCY TRANSLATION

Monetary assets and liabilities denominated in foreign currencies are translated at the rate notified by the European Central Bank (euro reference rate) as at the balance sheet date. Non-monetary items measured at historic acquisition costs in a foreign currency are to be translated at the exchange rate on the day of the transaction; non-monetary items measured at fair value in a foreign currency are to be translated at the exchange rate of the day on which the value was determined. Results from currency translation are recognised in the Income Statement under the “Net trading and valuation result”. In the case of available-for-sale instruments, the translation result from fair value measurement through equity is reported in comprehensive income.

7. LOANS AND RECEIVABLES

Loans and receivables are non-derivative financial assets with fixed and/or determinable cash flows, which are not quoted in an active market. Assets of this category are recognised on the Balance Sheet under “Loans and advances to banks”, “Loans and advances to customers” and “Cash and balances with central banks”. Initially, these assets are measured at fair value, taking account of transaction costs. Arrangement fees are distributed over the term of the underlying transaction at constant effective interest. Subsequently, the assets are measured at amortised cost. Amortised cost is derived from the distribution of differences between the issuing price and the amount repayable at constant effective interest, reduced by impairment charges, if any. The result of the amortisation of differences at constant effective interest is recognised in the Income Statement under “Net interest income”. The accounting treatment of loans and receivables as underlyings in hedge accounting is explained in Note 15.

8. RISK PROVISIONS

Risk provisions for loans and advances comprise impairments (for on-balance-sheet lending business) and provisions (for off-balance-sheet lending business), unless designated as at fair value. Changes in risk provisions for loans and advances not measured at fair value are booked on a separate account and recognised under “Loan impairment”. Provisions for risks in the securities business reduce the book value and are booked recognised in the “Net trading and valuation result”.

Impairments are recognised in the amount of the difference between the book value of the financial asset and the net present value of the expected future cash flows, discounted at the original effective interest rate of the financial asset (IAS 39.63). Additionally, impaired assets accounted for at amortised cost are booked on a non-interest basis, with contractually agreed interest income no longer recognised. Instead, interest income is determined by adding unaccrued interest to the present value of the cash flows expected over the reporting period at the effective interest rate originally used to calculate the impairment loss (IAS 39 A93). Once it has been established that no payment will be received, the receivable is derecognised.

A multi-stage risk control process is used to identify, monitor and manage counterparties with increased credit risks; all exposures/counterparties are classified according to four risk classes.

- **Risk class 0**: Regular transaction
  Standard risk class for all exposures without irregularities and not belonging to any of the following risk classes.

- **Risk class 1**: Intensive management – performing
  Counterparties with increased credit risk and/or other irregularities and therefore subject to close monitoring (intensive management). However, these counterparties are not considered to be at risk of default and no specific loan loss provisions need to be booked.

- **Risk class 2**: Workout – restructuring
  Exposures in workout classified as restructuring cases.

- **Risk class 3**: Workout – resolution
  Exposures for which restructuring is not expected to produce the desired result and recovery measures are taken instead.

Starting from risk class 1, provisioning requirements are reviewed monthly (impairment test). Specific loan loss provisions are to be set up if partial or full recovery of an amount owed, including interest, is considered unlikely. In any case, the possibility of specific loan loss provisioning is to be examined as soon as an exposure meets at least one of the following criteria:

- Interest waived due to the counterparty’s rating
- Significant credit risk adjustment, e.g.:
  - Rating downgrade to B range or lower
  - Default rating by an external rating agency
  - Reduction of current market price by more than 25%
  - Termination and call of receivable due to counterparty’s rating
- Concessions granted for reasons of counterparty’s rating (forbearance)
- Insolvency proceedings or similar proceedings have been instituted, or commencement of bankruptcy proceedings has been rejected for lack of assets, or the debtor as a legal person has been wound up by decision of a court or an administrative authority.
- Significant negative information available
- Payment arrears of 90 days, with the receivable past due exceeding the approved and communicated overall limit by more than 2.5%, but at least by EUR 250.0.

In addition to specific loan loss provisions, a portfolio loan loss provision is calculated for “incurred but not reported losses” according to IAS 39.64. To determine the provisioning requirement, the financial assets are broken down by risk profile into comparable groups. On the basis of empirical values and the bank’s monitoring processes, portfolio loan loss provisions are set up for these groups, the parameters considered being “loss identification period” (LIP), “probability of default” and “loss given default”.

9. ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

In principle, Kommunalkredit designates receivables and securities as at fair value through profit or loss in order to avoid or significantly diminish the incongruences that occur in the measurement or recognition of assets when their gains or losses are measured or recognised on a different basis (accounting mismatch), or when assets are managed, measured and reported to the management on a fair value basis. They are initially recognised and subsequently measured at fair value. The results are recognised in the Income Statement in the "Net trading and valuation result".

10. DERIVATIVES

The main purpose of derivatives at Kommunalkredit is to hedge the risk of interest rate changes and/or currency risks.

The derivatives items on the balance sheet comprise derivatives in hedges (fair value hedges) and other derivatives.

Derivatives are recognised at their fair value. Positive fair values are reported as assets under "Derivatives"; negative fair values are reported as liabilities under "Derivatives". Changes in the value of these derivatives based on the clean price are shown in the Income Statement in the "Net trading and valuation result", whereas interest income and expenses are recognised in gross interest income.

An embedded derivative is part of a compound financial instrument which also comprises a non-derivative host contract. Therefore, parts of the cash flows of the compound financial instrument are subject to similar fluctuations as a stand-alone derivative. An embedded derivative is recognised separately from the host contract and on the basis of derivative rules only if its economic features and risks are not closely related with the economic features and risks of the host contract, a stand-alone instrument with the same contractual terms would meet the definition of a derivative, and the compound financial instrument is not measured at fair value through profit or loss.

The fair values of derivatives are measured according to IFRS 13, as explained in detail in Note 14.

11. ASSETS HELD TO MATURIY

This balance sheet item comprises non-derivative financial assets with fixed or determinable cash flows and a fixed term, traded in active markets at the time of purchase or origination, which Kommunalkredit has the intention and ability to hold until maturity. Initial recognition is at fair value, taking account of transaction costs, with subsequent measurement at amortised cost. If acquisition costs differ from the repayable amount, the difference is recognised at constant effective interest under interest income. If the impairment test to be performed at regular intervals (see Note 8) indicates an impairment of held-to-maturity assets, the asset is written down to the extent necessary and recognised in the "Net trading and valuation result".

Financial instruments of the "assets held to maturity" category are recycled to the "assets available for sale" category, if classification of a financial investment as held to maturity is no longer justified in the absence of the intention or ability to hold such instruments to maturity. If more than an insignificant part of held-to-maturity investments is sold or reclassified, all assets of this category held by the Group are reclassified to the "assets available for sale" category. Consequently, financial instruments must not be classified as "assets held to maturity" in the current financial year and the two following financial years (tainting). In the event of recycling to the "assets available for sale" category, revaluation is performed at fair value, with the difference between the book value and the fair value recognised in equity (available-for-sale reserve). Currently, Kommunalkredit does not hold any assets of this measurement category.

12. ASSETS AVAILABLE FOR SALE

Financial instruments are classified as assets available for sale if they are to be held for an indefinite period of time and do not belong to the loans-and-receivables, held-to-maturity or fair-value-through-profit-or-loss (fair value option) categories.

Financial instruments of this category are initially recognised and subsequently measured at their fair values, with transaction costs taken into account. Changes in valuation are recognised in the Statement of Comprehensive Income and directly change the available-for-sale reserve (AFS reserve) within equity.

If the asset is sold or otherwise derecognised, the amount previously included in the AFS reserve carries through profit or loss (recycling). Interest earned on AFS financial instruments is recognised in net interest income, while dividends are reported under “Income from other investments”. The result of the sale or derecognition is recognised in the “Net trading and valuation result”. Any difference between the acquisition cost and the repayable amount is distributed proportionately over time at effective interest and recognised in net interest income. For details on the accounting of assets available for sale representing underlying transactions of hedges, see Note 15.

If the impairment test to be performed at regular intervals indicates impairment of AFS assets, the AFS reserve is recognised at fair value as an expense in the “Net trading and valuation result” in the Income Statement. If the grounds for impairment no longer apply, the impairment is reversed and the debt instrument is again recognised in the Income Statement up to its amortised cost. Amounts in excess of amortised cost are recognised in the AFS reserve. If equity instruments are no longer impaired, the impairment charges recognised in the Income Statement do not carry through profit or loss.

13. FINANCIAL GUARANTEES

A financial guarantee is a contract under which the guarantor is obliged to make certain payments to compensate the beneficiary of the guarantee for any losses arising from the failure of a debtor to make payments on schedule and according to the terms and conditions of a debt instrument. The potential obligation to pay is recognised according to IAS 39, as soon as Kommunalkredit becomes a contracting party. Initial measurement is at fair value. In an arm’s length transaction, the fair value corresponds either to the premium obtained upon conclusion of the contract, or a value of zero if no premium was paid upon conclusion of the contract, the assumption being an equivalence of service and consideration. Within the framework of subsequent measurement, the need for a provision according to IAS 37 is examined. If Kommunalkredit is the beneficiary of the guarantee, the guarantee is not recognised on the Balance Sheet.

Premiums received and paid are accounted for on an accrual basis and recognised in the Income Statement in “Net fee and commission income”.

14. FAIR VALUE MEASUREMENT

The fair value according to IAS 39 in conjunction with IFRS 13 is measured on the basis of the fair value hierarchy according to IFRS 13.72 (see also Note 67).

If the conditions of an active market are fulfilled, prices quoted in an active market are used for the measurement of **securities**. If no prices are quoted, the credit spread of comparable instruments is used to establish the fair value. If there is no active market, the fair value is measured using generally accepted, prevailing measurement methods on the basis of observable data. If necessary, these data are adjusted through risk premiums. If no observable inputs are available, reference is made to non-observable data (e.g. parameter estimates). If none of these measurement options can be applied, indicative third-party prices or expert estimates are used for fair value measurement.

Loans are measured by means of an internal measurement model based on the discounted-cash-flow method. The expected cash flows are discounted on the basis of current yield curves, considering the prevailing credit spreads. If the cash flows are non-deterministic, modelling is based on the optional conditions regarded as economically material.

In the case of regional and local territorial authorities (legacy portfolio), credit spreads are determined on the basis of margins for matching maturities. These margins are observed in the market on the basis of near-time transactions and comparative offers in the corresponding loan segments and factored in by maturity for different segments and rating classes. In the case of project finance, an individual credit spread is determined for each tranche. If available, Kommunalkredit uses margin information from the primary and secondary markets as well as expert estimates. To determine the credit spread for a facility, a sector-specific spread (sector benchmark spread) is referred to, which is then adjusted by premiums and discounts derived from catalogues of criteria reflecting the specific features of the project to be assessed. Spread assessment teams, supported by Risk Controlling, Banking, Syndication and Credit Risk, discuss each project and, if necessary, make additional adjustments based on updated information. This procedure, coordinated across the bank, results in the determination of credit spreads which reflect the risk of a transaction as truly as possible.

Derivatives are measured by means of an internal measurement model based on the discounted-cash-flow method, which takes current yield and basis spread curves into account. Embedded options are measured by means of the usual option measurement models (e.g. Hull-White, Dupire, Libor market model).

OIS curves (overnight index swaps) are used for the discounting of cash flows from OTC (over-the-counter) derivatives. When measuring interest-sensitive products with variable indicators, yield curves with different basis spread premiums are used, depending on the indicator (e.g. 3-month LIBOR, 9-month LIBOR, 12-month LIBOR). These refer to the indicator concerned and are used to derive forward rates for cash flow determination.

For derivatives in several currencies (e.g. cross-currency swaps), a cross currency basis is applied according to prevailing market standards, in addition to the adaptation of forwards by basis swap spreads. In simple trades, the OIS discount factor curve of the leg not corresponding to the collateral currency is aligned with the collateral currency through cross currency basis spreads. In trades with a more complex structure, the cross currency basis is also considered in the calculation of cash flows.

According to IFRS 13, counterparty default risk and own credit risk (credit value adjustment and debt value adjustment) are to be taken into account in measuring the fair value of derivatives. Both components are shown as BCVA (bilateral CVA = CVA-DVA). Kommunalkredit determines BCVA for all derivatives without bilateral daily cash collateral margin calls. For collateralised derivatives with bilateral daily cash collateral margin calls BCVA is considered to be immaterial. BCVA is calculated by the potential exposure method (based on Monte Carlo simulations) at counterparty level according to IFRS 13.48.

15. HEDGE ACCOUNTING

IAS 39 contains special provisions on hedge accounting, which are intended to prevent economically unjustified effects of measurement differences in hedged underlying transactions and hedging instruments on the Income Statement. The purpose of the hedge accounting rules is to recognise value changes of hedging instruments and the transactions hedged as mutually offsetting. In order to apply the hedge accounting rules, it is necessary to provide evidence of an effective hedging relationship between the underlying transaction and the hedging transaction. A hedging relationship is considered effective if the results of the hedging instrument and the results of the hedged underlying transaction – relative to the risk hedged – offset each other within a range of 80% to 125%. At Kommunalkredit, compliance with these conditions is verified through prospective (cross-checking of the components determining the market value) and retrospective effectiveness tests.

The prospective effectiveness test compares all parameters of the underlying transaction and the hedging transaction that determine the extent of the hedged change in value and verifies whether the hedged fair value of the structure (underlying and hedging transactions) fluctuates within a range of 80% to 125% maximum.

The retrospective effectiveness test checks if the hedged fair value of the structure (underlying and hedging transactions) fluctuated within a range of not more than 80% and 125%.

The fair value hedge applied by Kommunalkredit serves to hedge the fair value of assets or liabilities. This type of hedge is used to hedge interest and/or currency risks. The hedging instruments used are interest-rate swaps and interest-rate cross-currency swaps. The derivative used as a hedging instrument is shown at its fair value, with measurement changes recognised in the Income Statement in the “Net trading and valuation result”. For the hedged asset or liability, the changes in fair value resulting from the hedged risk are recognised in the same Income Statement item. On the Balance Sheet, the measurement result corresponding to the hedged risk is recognised in the same item as the underlying transaction.

The cash flow hedge serves to hedge the risk of fluctuating cash flows of the underlying assets. This type of hedge accounting is used to hedge cash flow changes resulting from interest-rate and currency risks. The hedging instrument used is the interest-rate cross-currency swap. The effective part of the derivative used as a hedging instrument is measured at fair value in comprehensive income (CFH reserve) and reported separately in the Statement of Comprehensive Income. The gains/losses recognised in equity are recycled to the Income Statement of the period in which the hedged transaction is realised. The hedged asset is recognised at amortised cost (loans-and-receivables category). Currently, Kommunalkredit does not use cash flow hedges to hedge the risk of fluctuating cash flows.

Hedge ineffectiveness is recognised in profit and loss. Kommunalkredit did not use the option of a fair value hedge of the interest rate exposure of a portion of a portfolio (according to IAS 39.89A). The possibility of hedging a net investment in a foreign business currently is of no relevance for Kommunalkredit.

16. CLASSES OF FINANCIAL INSTRUMENTS

In accordance with the requirement to group financial instruments into classes of similar instruments within the framework of the Notes to the Financial Statements (IFRS 7.6), Kommunalkredit distinguishes the following classes of financial instruments:

Classes of financial instruments	Accounting treatment
Cash and balances with central banks	Amortised cost
Financial assets	
At fair value through profit or loss: held for trading	Fair value
At fair value through profit or loss: fair value option	Fair value
Held to maturity	Amortised cost
Loans and receivables: loans and advances to banks	Amortised cost
Loans and receivables: loans and advances to customers	Amortised cost
Available for sale	Fair value

Classes of financial instruments	Accounting treatment
Financial liabilities	
At amortised cost	Amortised cost
At fair value through profit or loss: fair value option	Fair value
At fair value through profit or loss: held for trading	Fair value
Derivatives designated as hedging instruments	Fair value
Contingent liabilities	Off-balance-sheet
Other off-balance-sheet liabilities	Off-balance-sheet

As at the balance sheet date, the following classes of financial instruments were not used by Kommunalkredit:

- Financial assets: held to maturity
- Financial liabilities: at fair value through profit or loss: fair value option

17. INVESTMENTS IN ASSOCIATES

Associates are accounted for under the equity method according to IAS 28 (Associates and Joint Ventures) (see also Note 5). The value of these investments is reviewed at every balance-sheet date on the basis of forecasts.

18. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment comprise land and buildings primarily for the company's own use as well as office furniture and equipment. Land is recognised at cost. Buildings as well as office furniture and equipment are measured at cost less straight-line depreciation. The assumed projected periods of use are:

- Buildings: 40 years
- Office furniture and equipment: 4 to 10 years
- IT investment: 3 to 4 years
- Works of art are not subject to straight-line depreciation.

In the event of indications of impairment, extraordinary write-offs are made if the book value is above the higher of net sales price or value in use. If the grounds for impairment no longer apply, reversals are booked up to the level of amortised cost.

19. INTANGIBLE ASSETS

Intangible assets exclusively comprise purchased software. Software is written off by the straight-line method over 3 years and recognised under general administrative expenses.

In the event of indications of impairment, extraordinary write-offs are made if the book value is above the higher of net sales price or value in use. If the grounds for impairment no longer apply, reversals are booked up to the level of amortised cost.

20. FINANCIAL LIABILITIES

Financial liabilities are initially recognised at fair value, with transaction costs being taken into account. Long-term bonds issued discounted (e.g. zero bonds) and similar liabilities are recognised marked up for interest accruing by means of the effective interest method. Currently, there are no liabilities in the fair value portfolio. For details on the accounting of liabilities representing underlying transactions in hedge accounting, see Note 15.

21. PROVISIONS

Provisions for pensions, severance pay and jubilee bonuses are calculated annually by an independent actuary according to the projected unit credit method in accordance with IAS 19. The "AVÖ 2008-P calculation bases for pension insurance – Pagler & Pagler", in their version for salaried employees, are used as a calculation basis. The actuarial discount rate was determined on the basis of the yields of prime fixed-income corporate bonds, with due consideration given to the terms of the obligations to be met.

The most important parameters applied in the calculation are:

- an actuarial discount rate of
  – 2.0% (31/12/2016: 2.0%) for pension obligations
  – 1.5% (31/12/2016: 1.5%) for obligations from severance pay and
  – 0.5% (31/12/2015: 0.5%) for obligations from jubilee bonuses
- an incremental rate of active salary and pension payments of 2%, unchanged from the previous year
- a career trend of 1.5%, unchanged from the previous year
- assumed pensionable ages of 60 for women and 65 for men, taking into account the transitional provisions of the 2003 Budget Framework Act and the provisions on age limits for women of the Act on Occupational Old-Age Provision
- a fluctuation discount on provisions for severance pay determined on the basis of statistically recorded leaves

All pension obligations to active employees have been transferred to a pension fund. The provisions reported therefore only contain entitlements from defined-benefit pension obligations for eight employees not covered by the pension fund, resulting from direct commitments within the framework of the collective bargaining agreement (1961 pension reform, as amended on 1 January 1997) made prior to the transfer to the pension fund, or from individual contracts. The pension plan is a defined-benefit plan under which benefits for active staff, relative to the risk of death and invalidity, depend on the salary earned. Benefits for staff reaching retirement age are already fixed and therefore only subject to adjustment in line with the annual increase agreed through collective bargaining. As the defined-benefit components are fully funded, supplementary allocations will only be required in the event of underperformance or “premature” payment of benefits.
The provision for pensions corresponds to the net present value of the defined-benefit obligation minus the fair value of the plan assets. Actuarial gains and losses based on empirically determined adjustments and changes of actuarial assumptions are immediately recognised in equity in comprehensive income. Other expenses are recognised in the Income Statement under “Personnel expenses” as part of general administrative expenses.

Provisions for severance pay are calculated by an independent actuary and set up according to the same actuarial principles to cover statutory and contractual entitlements. Actuarial gains and losses are subject to the same accounting treatment as pension obligations.

For other long-term employee benefits, i.e. jubilee bonus entitlements, a jubilee bonus provision, calculated according to the same principles, is set up. Actuarial gains and losses are immediately recognised in personnel expenses and carry through profit or loss.

22. CURRENT AND DEFERRED TAX ASSETS

Taxes on income are recognised and calculated in accordance with IAS 12.

Current income-tax assets and liabilities are measured at current tax rates. Tax claims are shown under “Current tax assets”, and tax payable under “Current tax liabilities”.

For the calculation of deferred taxes, all temporary differences are taken into account. Under this concept, the assets and liabilities recognised on the balance sheet according to IFRS are compared with the taxable amounts of the consolidated company in question. Temporary differences between the amounts recognised lead to differences in value, for which deferred tax assets or liabilities must be reported – irrespective of the time of their release. Deferred tax assets and deferred tax liabilities for the same term are offset if they exist against the same tax creditor.

Tax loss carryforwards are recognised as tax assets if they can be reasonably expected to be used in the near future. The possibility of using tax loss carryforwards is reviewed annually on the basis of the Group’s tax budgeting process.

Effective as of 2016, a tax group pursuant to § 9 of the Corporate Income Tax Act was formed, with Satere Beteiligungsverwaltungs GmbH as the group parent and Gesona Beteiligungsverwaltung GmbH, Kommunalkredit, KBI, KPC and TrendMind IT Dienstleistung GmbH (TrendMind) as group members. On the basis of a group and tax contribution agreement, the stand-alone method was chosen for the calculation of the tax contributions. According to this method, the amount of the tax contributions of the group members depends on the amount of corporate income tax the group member would have had to pay if its tax result had not been counted toward the group parent. Tax loss carryforwards of a group member from periods prior to the formation of the group (pre-group losses) are credited up to the amount of the profit of the group member and diminish the tax contribution of the group member.

If a group member's negative income is counted toward the group parent, this tax loss is kept on record for the group member (internal loss carryforward) and netted against the positive income of the group member in subsequent years up to 100%. Upon termination of the tax group or elimination of a group member, a final compensation has to be paid for tax losses not yet reimbursed, multiplied by the corporate tax rate applicable at the time of termination of the agreement.

23. DERECOGNITION OF FINANCIAL ASSETS AND LIABILITIES

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset have expired or when the Group has transferred such rights, including all material risks and rewards of ownership. If all risks and rewards are neither transferred nor retained, derecognition of the asset depends on whether control over the asset is transferred.

If the Group retains all substantial risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset as well as a collateralised financial instrument for the consideration received.

A financial liability is derecognised upon redemption, i.e. when its contractual obligations have been discharged or are cancelled or expire, or when a financial liability is replaced by a liability against the same lender under significantly different contractual terms.

Upon complete derecognition of a financial instrument, the difference between the book value and the sum total of the consideration received or to be received and all accumulated gains or losses, which have been recognised in comprehensive income and accumulated in equity, are recognised in the Income Statement.

24. SIGNIFICANT ESTIMATES AND JUDGMENTS

The preparation of financial statements according to IFRS requires management to make judgements, estimates and assumptions regarding certain categories of assets and liabilities. Areas in which such estimates and judgements are required include, in particular, the setting up of risk provisions (see Note 8), the determination of the fair value of financial assets and liabilities (see Note 14), the measurement of provisions (see Note 21), the recognition and measurement of deferred tax assets (see Note 22), and the assessment of legal risks (see Note 69).

These judgments and estimates influence the recognition of assets and liabilities, contingent claims and contingent liabilities on the balance sheet date, and of income and expenses of the reporting period. Management holds regular meetings to review its judgments and estimates. Decisions are taken by the competent bodies of the bank and documented accordingly. The underlying assumptions are continuously reviewed and recorded. Actual results may differ from management estimates.

BALANCE SHEET DISCLOSURES OF THE KOMMUNALKREDIT GROUP

25. CASH AND BALANCES WITH CENTRAL BANKS

in EUR 1,000	31/12/2017	31/12/2016
Cash on hand	9.1	6.0
Balances with central banks	318,100.0	310,451.4
Total	**318,109.1**	**310,457.4**

26. LOANS AND ADVANCES TO BANKS (LOANS AND RECEIVABLES)

in EUR 1,000	31/12/2017	31/12/2016
Repayable on demand	101,809.8	101,865.39
Other receivables	38,387.7	0.0
Total	**140,197.5**	**101,865.4**

Loans and advances to banks repayable on demand include cash and cash equivalents provided as cash collateral for negative market values of derivatives according to ISDA/CSA arrangements in the amount of TEUR 87,362.2 (31/12/2016: TEUR 91,030.6) and positive balances with credit institutions in the amount of TEUR 14,397.6 (31/12/2016: TEUR 10,784.8). Other receivables exclusively include collateral for disbursement obligations arising from loan contracts.

27. LOANS AND ADVANCES TO CUSTOMERS (LOANS AND RECEIVABLES)

in EUR 1,000	31/12/2017	31/12/2016
Repayable on demand	97,213.9	43,070.6
Other receivables	1,995,114.1	2,096,006.4
Portfolio loan loss provision	-448.4	-148.0
Total	**2,091,879.7**	**2,138,929.0**

Loans and advances to customers repayable on demand include cash and cash equivalents provided as collateral for negative market values of derivatives (transactions with non-bank financial institutions) according to ISDA/CSA arrangements in the amount of TEUR 97,079.0 (31/12/2016: TEUR 43,050.0).

Other receivables mainly include loans to customers with a book value of TEUR 1,641,945.0 (31/12/2016: TEUR 1,699,201.6) and securities of the loans-and-receivables category with a book value of TEUR 353,294.1 (31/12/2016: TEUR 386,667.0).

27.1 Loan loss provisions

Loan loss provisions recognised in loans and advances to customers are booked on a separate allowance account and developed as follows:

Development of loan loss provisions in EUR 1,000		2017	2016
as at 1/1		**148.0**	**212.5**
Additions			
	Additions to loan loss provisions	300.4	0.0
	of which specific allowances according to IAS 39.63	*0.0*	*0.0*
	of which portfolio allowances according to IAS 39.64	*300.4*	*0.0*
Reversals			
	Reversal of loan loss provisions	0.0	-64.6
	of which specific allowances according to IAS 39.63	*0.0*	*0.0*
	of which portfolio allowances according to IAS 39.64	*0.0*	*-64.6*
	Earmarked use	0.0	0.0
as at 31/12		**448.4**	**148.0**

As in the previous year, no specific loan loss provisions had to be set up in 2017. The non-performing loan ratio remains unchanged at 0.0%. The portfolio allowance, considering the parameters “loss identification period (LIP)”, “probability of default” and loss given default” according to IAS 39.64, was increased by TEUR 300.4 in 2016 and amounted to TEUR 448.4 as at 31 December 2017 (31/12/2016: TEUR 148.0) For details, see Note 8 “Risk Provisions”.

27.2 Forbearance

Forbearance exposures are exposures to counterparties at risk of no longer being able to meet their payment obligations.

On account of the quality of its portfolio and/or its credit risk profile, forbearance practices are of minor importance at Kommunalkredit. In Kommunalkredit’s entire portfolio, a single counterparty in risk class 1, rated “BB+”, with a book value of TEUR 6,122.4 (31/12/2016: TEUR 6,681.0) was classified as a forbearance exposure (“forbearance performing”) as at 31 December 2017.

28. ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

in EUR 1,000	31/12/2017	31/12/2016
Loans to customers	583,023.6	664,405.2
Other bonds (non-listed)	22,707.5	27,210.7
Total	**605,731.1**	**691,616.0**

For details on fair value measurement, see Note 14. For a classification based on the categories of the fair value hierarchy according to IFRS 13.72 and a detailed description, see Note 67.

29. ASSETS AVAILABLE FOR SALE

in EUR 1,000	31/12/2017	31/12/2016
Public-sector bonds	201,762.3	127,803.9
of which exchange-listed	*201,762.3*	*116,974.7*
of which non-listed	*0.0*	*10,829.2*
Other bonds	6,991.8	15,531.4
of which exchange-listed	*6,991.8*	*15,531.4*
Variable-interest securities and interests	2,810.1	3,615.1
of which non-listed	*2,810.1*	*3,615.1*
Total	**211,564.2**	**146,950.4**

For details on fair value measurement, see Note 14. For a classification based on the categories of the fair value hierarchy according to IFRS 13.72 and a detailed description, see Note 67.

30. DERIVATIVES

At Kommunalkredit, derivatives primarily serve to hedge interest rate and/or currency risks. The positive fair values (for details on fair value measurement, see Note 14) of derivative financial instruments, shown on the asset side, are as follows (interest deferrals included):

in EUR 1,000	31/12/2017	31/12/2016
Interest-related transactions	231,392.0	318,641.8
of which fair-value hedges	*220,905.0*	*309,808.0*
Currency-related transactions	1,224.8	18,514.6
of which fair-value hedges	*923.1*	*855.6*
Total	**232,616.8**	**337,156.4**

The structure of the derivative financial instruments, including their market values, is shown in Note 64.

31. INVESTMENTS IN ASSOCIATES

After the impairment booked in 2016, the book value of the investment in Kommunalleasing GmbH remains unchanged at TEUR 0.0. Non-recognised losses for this at-equity investment are shown neither in the reporting year nor on a cumulative basis.

As at 31 December 2017, the assets and liabilities of this company amounted to TEUR 81,191.2 (31/12/2016: TEUR 91,071.5) and TEUR 76,004.2 (31/12/2016: TEUR 86,011.1), respectively; revenues for the reporting period amounted to TEUR 491.3 (1/1-31/12/2016: TEUR 609.5), and the profit for the year according to IFRS came to TEUR 126.6 (1/1-31/12/2016: TEUR 415.6).

32. PROPERTY, PLANT AND EQUIPMENT

The development and composition of property, plant and equipment is shown in Note 34 (Schedule of Non-current Asset Transactions). The value of land and buildings used by the Group, as shown on the Balance Sheet, is unchanged from the previous year and includes a land value of TEUR 3,961.1.

in EUR 1,000	31/12/2017	31/12/2016
Land and buildings	23,302.6	24,058.9
Office furniture and equipment	2,547.7	2,855.4
Facilities under construction	0.0	26.6
Total	**25,850.3**	**26,940.9**

33. INTANGIBLE ASSETS

This balance sheet item exclusively comprises purchased software. For its development and composition, see Note 34 (Schedule of Non-current Asset Transactions).

34. SCHEDULE OF NON-CURRENT ASSET TRANSACTIONS

The Schedule of Non-current Asset Transactions shows the development and composition of property, plant and equipment and non-current intangible assets.

As at 31 December 2017, the Schedule of Non-current Asset Transactions is as follows:

Schedule of non-current asset transactions 2017 in EUR 1,000	Acquisition costs					Cumulative depreciation and amortisation					
	as at 1/1/2017	Additions	Disposals	Transfers	as at 31/12/2017	as at 1/1/2017	Additions	Disposals	as at 31/12/2017	Book value 31/12/2017	Book value 31/12/2016
Property, plant and equipment	**44,752.7**	**468.2**	**-44.6**	**0.0**	**45,176.3**	**17,811.8**	**1,558.6**	**-44.4**	**19,326.0**	**25,850.3**	**26,940.9**
Land and buildings	37,453.0	127.9	0.0	26.6	37,607.5	13,394.1	910.8	0.0	14,304.9	23,302.6	24,058.9
Office furniture and equipment	7,273.1	340.3	-44.6	0.0	7,568.8	4,417.7	647.8	-44.4	5,021.1	2,547.7	2,855.4
Facilities under construction	26.6	0.0	0.0	-26.6	0.0	0.0	0.0	0.0	0.0	0.0	26.6
Intangible assets	**4,415.1**	**123.9**	**0.0**	**0.0**	**4,539.0**	**4,126.3**	**221.3**	**0.0**	**4,347.6**	**191.4**	**288.7**
Total of property, plant and equipment and intangible assets	**49,167.8**	**592.1**	**-44.6**	**0.0**	**49,715.3**	**21,938.1**	**1,779.9**	**-44.4**	**23,673.7**	**26,041.7**	**27,229.6**

Schedule of non-current asset transactions 2016 in EUR 1,000	Acquisition costs					Cumulative depreciation and amortisation					
	as at 1/1/2016	Additions	Disposals	Transfers	as at 31/12/2016	as at 1/1/2016	Additions	Disposals	as at 31/12/2016	Book value 31/12/2016	Book value 31/12/2015
Property, plant and equipment	**44,298.3**	**1,033.5**	**-579.2**	**0.0**	**44,752.7**	**16,640.8**	**1,751.8**	**-580.9**	**17,811.8**	**26,940.9**	**27,657.5**
Land and buildings	37,168.4	21.6	0.0	263.1	37,453.0	12,497.0	897.1	0.0	13,394.1	24,058.9	24,671.4
Office furniture and equipment	6,868.5	985.4	-580.9	0.0	7,273.1	4,143.8	854.7	-580.9	4,417.7	2,855.4	2,724.7
Facilities under construction	261.4	26.6	1.7	-263.1	26.6	0.0	0.0	0.0	0.0	26.6	261.4
Intangible assets	**4,240.3**	**174.8**	**0.0**	**0.0**	**4,415.1**	**3,856.7**	**269.6**	**0.0**	**4,126.3**	**288.7**	**383.6**
Total of property, plant and equipment and intangible assets	**48,538.6**	**1,208.3**	**-579.2**	**0.0**	**49,167.8**	**20,497.5**	**2,021.5**	**-580.9**	**21,938.1**	**27,229.6**	**28,041.1**

35. TAX ASSETS

in EUR 1,000	31/12/2017	31/12/2016
Current tax assets	476.5	3,249.1
Deferred tax assets	27,243.6	15,841.2
Total	**27,720.1**	**19,090.2**

Deferred tax assets and liabilities include taxes arising from temporary differences between valuations according to IFRS and the calculation of the Group's taxable profit. The origin and development of deferred taxes assets is shown in the following table:

in EUR 1,000	as at 31/12/2016	Recognised in profit or loss	Recognised in equity	as at 31/12/2017
Deferred taxes from temporary differences in asset items				
Tax loss carryforwards	21,917.7	9,476.2	0.0	31,394.0
Loans and advances to banks	0.0	-8.7	0.0	-8.7
Loans and advances to customers	-17,611.6	6,197.3	0.0	-11,414.4
Assets at fair value	-38,357.3	6,005.8	0.0	-32,351.5
Assets available for sale	-2,392.7	1,643.8	132.8	-616.2
Derivatives	-69,886.6	19,623.0	0.0	-50,263.6
Investments in associates	160.7	-26.8	0.0	133.9
Property, plant and equipment	0.0	-11.4	0.0	-11.4
Deferred taxes from temporary differences in liability items				
Amounts owed to banks	0.0	-374.5	0.0	-374.5
Amounts owed to customers	4,376.2	-3,540.3	0.0	835.9
Derivatives	55,393.0	-11,731.7	0.0	43,661.3
Securitised liabilities	60,695.6	-15,804.5	0.0	44,891.1
Subordinated liabilities	579.8	-231.1	0.0	348.7
Provisions	966.4	0.0	-87.5	878.9
Other liabilities	0.0	140.0	0.0	140.0
Total	**15,841.2**	**11,357.1**	**45.3**	**27,243.6**

The comparative figures as at 31 December 2016 are as follows:

in EUR 1,000	as at 31/12/2015	Recognised in profit or loss	Recognised in equity	as at 31/12/2016
Deferred taxes from temporary differences in asset items				
Tax loss carryforwards	12,801.0	9,116.8	0.0	21,917.7
Loans and advances to banks	0.0	0.0	0.0	0.0
Loans and advances to customers	-17,182.8	-428.9	0.0	-17,611.6
Assets at fair value	-40,842.9	2,485.5	0.0	-38,357.3
Assets available for sale	-3,841.7	1,353.3	95.7	-2,392.7
Derivatives	-120,334.9	50,448.3	0.0	-69,886.6
Investments in associates	0.0	160.7	0.0	160.7
Deferred taxes from temporary differences in liability items				
Amounts owed to banks	0.0	0.0	0.0	0.0
Amounts owed to customers	3,704.0	672.2	0.0	4,376.2
Derivatives	83,857.6	-28,464.6	0.0	55,393.0
Securitised liabilities	81,076.2	-20,380.7	0.0	60,695.6
Subordinated liabilities	1,580.7	-1,001.0	0.0	579.8
Provisions	958.5	-25.0	32.9	966.4
Total	**1,775.8**	**13,936.7**	**128.7**	**15,841.2**

The asset item booked for deferred tax assets in the amount of TEUR 27,243.6 (31/12/2016: TEUR 15,841.2) comprises TEUR 31,394.0 (31/12/2016: TEUR 21,917.7) in capitalised tax loss carryforwards and TEUR -4,150.4 (31/12/2016: TEUR -6,076.5) in temporary differences, as shown in the above table.

Of the tax loss carryforwards as at 31 December 2017 in the amount of TEUR 128,642.6 (31/12/2016: TEUR 145,577.4), an amount of TEUR 125,576.0 (31/12/2016: TEUR 87,670.8) was taken into account due to its probable use in the near future based on tax budgeting. Given a tax rate of 25%, this resulted in an asset item of TEUR 31,394.0 (31/12/2016: TEUR 21,917.7). The tax assets correspond to the planned future use of the tax loss carryforward of Kommunalkredit, considering the formation of a tax group pursuant to § 9 of the Corporate Income Tax Act with Satere Beteiligungsverwaltungs GmbH as the group parent in 2016 (for details see Note 22).

Given a tax rate of 25%, the use of tax loss carryforwards in the reporting year amounted to TEUR 4,001.6 (2016: TEUR 13,768.5).

The capitalised tax loss carryforward of TEUR 31,394.0 as at 31 December 2017 is to be realised within the coming twelve months in an amount of TEUR 3,293.4. The balance of TEUR 28,100.6 is expected to be used in the following four years.

There are no plans to realise deferred tax assets resulting from financial instruments and provisions (apart from measurement effects and maturities) within the coming twelve months. Current tax assets arising from current tax accounting are of a short-term nature.

36. OTHER ASSETS

in EUR 1,000	31/12/2017	31/12/2016
Other assets	8,339.5	16,086.0
Accruals/deferrals	1,030.9	1,424.5
Total	**9,370.4**	**17,510.6**

Other assets comprise the following material items: receivables for services invoiced to KA Finanz AG in the amount of TEUR 3,678.8 (31/12/2016: TEUR 10,504.1), trade receivables in the amount of TEUR 2,244.9 (31/12/2016: TEUR 2,599.7), interest receivable in the amount of TEUR 1,405.2 (31/12/2016: TEUR 1,561.9), receivables from the settlement of payments under support programmes in the amount of TEUR 353.4 (31/12/2016: TEUR 684.5).

Accruals/deferrals mainly comprise fees and other administrative expenses recognised according to the accruals concept.

37. AMOUNTS OWED TO BANKS

in EUR 1,000	31/12/2017	31/12/2016
Repayable on demand	114,768.3	226,607.0
Other liabilities	418,069.9	568,420.9
Total	**532,838.2**	**795,027.9**

Amounts owed to banks repayable on demand include cash and cash equivalents received as cash collateral for positive market values of derivatives according to ISDA/CSA arrangements in the amount of TEUR 96,216.0 (31/12/2016: TEUR 216,491.6). Other liabilities to banks include TEUR 312,431.8 (31/12/2016: TEUR 313,930.0) in medium-term funds from the TLTRO II programme (Targeted Longer-Term Refinancing Operations) of the European Central Bank (ECB) and TEUR 62,209.4 (31/12/2016: TEUR 64,638.9) in collateralised loans of the European Investment Bank.

38. AMOUNTS OWED TO CUSTOMERS

Amounts owed to customers in EUR 1,000	31/12/2017	31/12/2016
Deposits by corporates, municipalities and quasi-municipal enterprises	528,760.9	210,826.3
Deposits by retail customers - KOMMUNALKREDIT INVEST	115,653.7	0.0
Cash collateral received for positive market values of derivatives	63,715.8	13.1
Other long-term liabilities to customers	329,892.6	341,253.6
Total	**1,038,002.0**	**552,093.0**

Amounts owed to customers include TEUR 212,325.1 (31/12/2016: TEUR 5,447.3) repayable on demand.

39. DERIVATIVES

Derivative transactions at Kommunalkredit mainly serve for the purpose of hedging interest rate and/or currency risks. The negative fair values of derivative financial instruments are reported on the liabilities side (for details on fair value measurement, see Note 14) and shown in the following table (including interest accruals/deferrals):

in EUR 1,000	31/12/2017	31/12/2016
Interest-related transactions	205,016.7	248,296.5
of which in fair-value hedges	*74,412.9*	*91,783.9*
Currency-related transactions	39,692.6	15,051.0
of which in fair-value hedges	*2,991.2*	*1,453.1*
Total	**244,709.4**	**263,347.5**

The structure of the derivative financial instruments, including their market values, is shown in Note 64.

40. SECURITISED LIABIITIES

in EUR 1,000	31/12/2017	31/12/2016
Bonds issued	947,323.0	1,169,155.8
Other securitised liabilities	521,259.1	610,009.6
Total	**1,468,582.1**	**1,779,165.4**

Bonds issued and other securitised liabilities comprise covered bonds issued by Kommunalkredit in a book value of TEUR 1,123,636.9 (31/12/2016: TEUR 1,362,141.7), which are collateralised by a cover pool. Besides covered bonds, this balance sheet item primarily includes senior unsecured bonds with long maturities. Securitised liabilities with a nominal value of TEUR 21,703.4 (2017: TEUR 318,171.7) will fall due in 2018.

41. SUBORDINATED LIABILITIES

As at 31 December 2017, subordinated liabilities were broken down as follows:

Type of liability	Interest rate 31/12/2017	Currency	Nominal in EUR 1,000	Book value in EUR 1,000
Subordinated bonded note 2007-2022	4.67%	EUR	10,000.0	11,538.2
Subordinated bonded note 2007-2022	4.67%	EUR	10,000.0	11,538.2
Subordinated bonded note 2007-2047	5.02%	EUR	10,000.0	9,910.0
Subordinated bonded loan 2007-2047	5.02%	EUR	9,000.0	8,919.0
Subordinated bonded note 2007-2037	5.08%	EUR	10,000.0	10,028.8
Subordinated bonded loan 2007-2037	5.08%	EUR	800.0	802.3
Subordinated bonded loan 2007-2037	5.08%	EUR	10,200.0	10,229.4
Subordinated bond 2006-2021	5.40%	EUR	5,000.0	5,956.3
Total			**65,000.0**	**68,922.1**

The comparative figures as at 31 December 2016 are as follows:

Type of liability	Interest rate 31/12/2016	Currency	Nominal in EUR 1,000	Book value in EUR 1,000
Subordinated bonded note 2007-2022	4.67%	EUR	10,000.0	11,812.8
Subordinated bonded note 2007-2022	4.67%	EUR	10,000.0	11,812.8
Subordinated bonded note 2007-2047	5.02%	EUR	10,000.0	9,961.3
Subordinated bonded loan 2007-2047	5.02%	EUR	9,000.0	8,965.1
Subordinated bonded note 2007-2037	5.08%	EUR	10,000.0	10,061.0
Subordinated bonded loan 2007-2037	5.08%	EUR	800.0	804.9
Subordinated bonded loan 2007-2037	5.08%	EUR	10,200.0	10,262.2
Subordinated bond 2006-2021	5.40%	EUR	5,000.0	6,166.6
Total			**65,000.0**	**69,846.8**

Kommunalkredit's subordinated liabilities add up to a nominal value of TEUR 65,000.0 (31/12/2016: TEUR 65,000.0) and a book value of TEUR 68,922.1 (31/12/2016: TEUR 69,846.8). The difference between the book value and the nominal value is due to hedge accounting according to IAS 39.

Interest expenses for all subordinated liabilities in the reporting period amounted to TEUR 2,674.5 (1/1-31/12/2016: TEUR 2,675.8). Creditor claims to repayment of these liabilities are subordinate in relation to other creditors and, in the event of bankruptcy or liquidation, will be fulfilled only after all non-subordinated creditors have been satisfied.

The subordinated liabilities meet the conditions of Part 2 Title I Chapter 4 of EU Regulation 575/2013 (CRR) and are eligible as additional regulatory capital.

42. PROVISIONS

As at 31 December 2017, provisions primarily included long-term provisions for personnel expenses. (For details on provisions, see also Note 21).

in EUR 1,000	Opening balance 1/1/2017	Changes: recognised in personnel expenses	Changes: recognised in other comprehensive income and/or equity	Closing balance 31/12/2017
Provisions for pensions	1,415.3	281.6	-121.2	1,575.7
Provisions for severance pay	6,063.3	425.6	-871.7	5,617.2
Provisions for jubilee bonuses	341.0	-65.3	0.0	275.7
Other provisions	0.0	125.6	0.0	125.6
Total	**7,819.6**	**767.5**	**-992.8**	**7.594.2**

The actuarial provisioning requirement for personnel expenses developed as follows in 2017:

in EUR 1,000		Provisions for: Pensions	Severance pay	Jubilee bonuses	Total
as at 31/12/2016					
Present value of defined benefit obligation					
DBO as at 31/12/2016		1,885.8	6,063.3	341.0	8,290.1
- plan assets		-470.5	0.0	0.0	-470.5
Actuarial provisioning requirement as at 31/12/2016		**1,415.3**	**6,063.3**	**341.0**	**7,819.6**
Current service cost		67.0	393.5	13.0	
Interest cost		37.7	88.6	1.6	
Actuarial gains (-) / losses (+) from DBO		-98.5	-871.7	-29.4	
of which due to changes in demographic assumptions		0.0	-522.3	0.0	
of which due to empirical changes		-98.5	-349.4	-29.4	
of which due to changes in financial assumptions		0.0	0.0	0.0	
Payments		0.0	-56.4	-50.6	
Other changes		186.3	0.0	0.0	
Change in DBO 2017		**192.5**	**-446.0**	**-65.4**	
Change in plan assets 2017		**-32.1**	**0.0**	**0.0**	
DBO as at 31/12/2017		2,078.3	5,617.2	275.7	7,971.2
- plan assets		-502.6	0.0	0.0	-502.6
Actuarial provisioning requirement as at 31/12/2017		**1,575.7**	**5,617.2**	**275.7**	**7,468.6**
Duration of DBO in years		19	11		
Sensitivity of DBO to change in actuarial interest rate by	plus 0.5%	-8.8%	-5.4%		
	minus 0.5%	10.1%	5.9%		
Sensitivity of DBO to deviation of salary development by	plus 0.5%		5.7%		
	minus 0.5%		-5.3%		
Sensitivity of DBO to deviation of pension increase by	plus 0.5%	8.3%			
	minus 0.5%	-7.4%			

The comparative figures as at 31 December 2016 are as follows:

in EUR 1,000	Opening balance 1/1/2016	Changes: recognised in personnel expenses	Changes: recognised in comprehensive income and/or equity	Closing balance 31/12/2016
Provisions for pensions	1,551.4	-102.6	-33.6	1,415.3
Provisions for severance pay	5,442.8	455.2	165.2	6,063.3
Provisions for jubilee bonuses	382.6	-41.5	0.0	341.0
Total	**7,376.9**	**311.1**	**131.6**	**7,819.6**

The actuarial provisioning requirement for personnel expenses developed as follows in 2016:

in EUR 1,000		Provisions for Pensions	Severance pay	Jubilee bonuses	Total
as at 31/12/2015					
Present value of defined benefit obligation					
DBO as at 31/12/2015		2,008.7	5,442.8	382.6	7,834.1
- plan assets		-457.3	0.0	0.0	-457.3
Actuarial provision requirement as at 31/12/2015		**1,551.4**	**5,442.8**	**382.6**	**7,376.9**
Current service cost		67.0	360.5	13.6	
Interest cost		40.7	94.7	2.5	
Actuarial gains (-) / and losses (+) from DBO		-30.6	165.2	5.5	
of which due to changes in demographic assumptions		*0.0*	*0.0*	*0.0*	
of which due to empirical changes		-135.1	-36.9	0.5	
of which due to changes in financial assumptions		104.5	202.1	4.9	
Payments		-200.0	0.0	-63.1	
Change in DBO 2016		**-122.9**	**620.4**	**-41.5**	
Change in plan assets 2016		**-13.2**	**0.0**	**0.0**	
DBO as at 31/12/2016		1,885.8	6,063.3	341.0	8,290.1
- plan assets		-470.5	0.0	0.0	-470.5
Actuarial provisioning requirement as at 31/12/2016		**1,415.3**	**6,063.3**	**341.0**	**7,819.6**
Duration of DBO in years		23	14		
Sensitivity of DBO to change in actuarial interest rate by	plus 0.5 %	-10.2%	-6.5%		
	minus 0.5 %	11.8%	7.1%		
Sensitivity of DBO to deviation of salary development by	plus 0.5 %		7.0%		
	minus 0.5 %		-6.4%		
Sensitivity of DBO to deviation of pension increase by	plus 0.5 %	8.3%			
	minus 0.5 %	-7.4%			

The following table shows the development of the fair value of plan assets:

Development of the fair value of plan assets in EUR 1,000	2017	2016
as at 1/1	**470.5**	**457.3**
Interest income	9.4	10.3
Actuarial result due to empirical changes	22.7	2.9
Changes in financial year	**32.1**	**13.2**
as at 31/12	**502.6**	**470.5**

The breakdown of assets by asset class is shown in the following table:

Breakdown of assets by asset class	31/12/2017	31/12/2016
Securities – euro	13.1%	7.7%
Securities – euro high yield	4.8%	6.6%
Securities – euro emerging markets	12.2%	13.0%
Securities euro corporate	9.1%	13.7%
Securities – non-euro	0.2%	0.3%
Equity instruments – euro	13.0%	13.0%
Equity instruments – non-euro	11.8%	11.2%
Equity instruments – emerging markets	10.9%	10.8%
Alternative investments	3.6%	3.5%
Real estate	4.5%	4.5%
Cash and cash equivalents	16.7%	15.9%
Total	**100.0%**	**100.0%**

As at 31 December 2017, no market prices were quoted in an active market for 9.6% of the plan assets (31/12/2016: 17.4%). For 2018, the following developments are expected for the defined-benefit pension plans, assuming there is no change in the calculation parameters:

Expected development DBO in EUR 1,000	
Defined Benefit Obligation (DBO) as at 1/1/2018	**2,078.3**
Expected current service cost	60.5
Expected interest cost	41.6
Expected payments	0.0
Expected actuarial result	-57.7
DBO as at 31/12/2018	**2,122.6**

Development of the fair value of plan assets in EUR 1,000	
Plan assets as at 1/1/2018	**502.6**
Expected interest income	10.1
Expected payments by pension fund	0.0
Expected contribution by employer	0.0
Expected actuarial result	0.2
Expected plan assets as at 31/12/2018	**512.9**

43. CURRENT TAX LIABILITIES

As at 31 December 2017, tax liabilities amounted to TEUR 599.8 (31/12/2016: TEUR 1,695.3), of which TEUR 37.3 (31/12/2016: TEUR 891.4) resulted from corporate income tax and TEUR 562.5 (31/12/2016: TEUR 803.9) from turnover tax and other tax accounting, thus being of a short-term nature.

44. OTHER LIABILITIES

in EUR 1,000	31/12/2017	31/12/2016
Accruals/deferrals	1,641.1	1,972.5
Other liabilities	17,216.8	23,058.0
as at 31/12	**18,857.9**	**25,030.5**

Accruals/deferrals mainly include income from guarantee fees and other fees accounted for under the accruals concept.

Other liabilities mainly include accruals/deferrals for personnel-related expenses and accruals/deferrals for audit, legal and consultancy expenses.

45. EQUITY

A. Development and composition

The share capital of Kommunalkredit as of 31 December 2017, unchanged from the previous year, amounts to EUR 159,491,290.16. Gesona Beteiligungsverwaltung GmbH (Gesona) holds 30,938,843 no-par-value shares, i.e. 99.78% of the shares; the Association of Austrian Municipalities holds 68,216 shares, i.e. 0.22% of the shares. Each no-par-value share represents an interest of EUR 5.14 in the share capital. There are no shares that have been issued but not fully paid in. By a resolution adopted by the Annual Shareholders' Meeting of 10 March 2017, the Executive Board was authorized to increase the share capital through the issue of up to 15,503,529 new no-par-value registered shares by a maximum amount of EUR 79,745,642.51 (authorized capital), subject to approval by the Supervisory Board, within a period of five years after registration of the amendment to the Articles of Association.

The development and composition of equity according to IFRS is shown under Section IV (Statement of Changes in Equity).

B. Dividend payment on equity / Profit distribution proposal

The Executive Board will propose to the Annual Shareholders' Meeting on 6 March 2018 that from the net profit of TEUR 30,922.4 reported in the financial statements of Kommunalkredit Austria AG prepared in accordance with the Austrian Company Code/Austrian Banking Act an amount of TEUR 11,500.0 be distributed and the balance of TEUR 19,422.4 be carried forward to new account.

C. Capital adequacy management and regulatory own funds

Kommunalkredit is subject to the own funds requirements pursuant to Article 92 CRR (CET 1 ratio 4.5%, core capital ratio 6%, total capital ratio 8%). Taking into account the capital conservation buffer, the anticyclical buffer and the surcharge from the supervisory review and evaluation process (SREP), a common equity tier 1 ratio of 6.05%, a core capital ratio of 7.65% and a total capital ratio of 9.85% are required. The statutory requirements were met at all times during the reporting year.

In the medium term, Kommunalkredit aims to achieve a core capital ratio of 15%. For operational supervision and control, a system of continuous monitoring has been set up and monthly reports are submitted to the Executive Board. Details on Kommunalkredit's equity management are described in Note 68 (Risk Management) in the paragraph "Securing Minimum Capital Adequacy" (ICAAP).

C.1. Regulatory group of credit institution

Kommunalkredit is part of a group of credit institutions whose parent is Satere Beteiligungsverwaltungs GmbH (Satere), which holds 100% of Gesona. Gesona owns 99.78% of Kommunalkredit. Given that both Satere and Gesona are to be classified as financial holding companies as defined in CRR, Kommunalkredit – pursuant to Art. 11 para. 2 and para. 3 CRR – is the only credit institution obliged to meet the requirements of Part 2 to 4 (Own Funds, Capital Requirements, Large Exposures), Part 6 (Liquidity) and Part 7 (Leverage) of CRR on a consolidated basis. Kommunalkredit also meets the definition of a superordinate credit institution pursuant to § 30 (5) of the Austrian Banking Act, which is responsible for compliance with the provisions of the Austrian Banking Act applicable to groups of credit institutions.

Besides Satere, Gesona and Kommunalkredit, Kommunalkredit KBI Immobilien GmbH, Kommunalkredit KBI Immobilien GmbH & Co KG and Kommunalkredit LTI Immobilien GmbH & Co KG, as providers of ancillary services, form part of the regulatory group of credit institutions.

Own funds and own funds requirements of the group of credit institutions pursuant to the Austrian Company Code/Austrian Banking Act, calculated in accordance with CRR, show the following composition and development:

Basis for calculation in EUR 1,000	pursuant to Art. 92 CRR 31/12/2017	pursuant to Art. 92 CRR 31/12/2016
Total risk exposure amount pursuant to Art. 92 CRR	991,206.5	688,040.0
of which credit risk	*871,504.6*	*525,947.5*
of which operational risk	*102,095.6*	*110,737.5*
of which CVA charge	*17,502.1*	*51,247.5*
of which default fund of a qualifying counterparty	*104.2*	*107.5*

Own funds	31/12/2017	31/12/2016
Common equity tier 1 after deductible items (CET 1)	225,661.4	226,191.5
Additional own funds after deductible items	64,195.6	64,832.9
Eligible own funds (tier 1 and tier 2)	**289,857.0**	**291,024.4**
Total capital ratio	29.2%	42.3%
Common equity tier 1 ratio	22.8%	32.9%

Own funds as shown in the above table include the 2017 results of the group companies in accordance with the Austrian Company Code/Austrian Banking Act in the amount of TEUR 11,159.3; the proposed dividend of TEUR 11,500.0 was deducted from own funds.

C.2. Regulatory own funds of Kommunalkredit Austria AG

Own funds and own funds requirements, as reported in the separate financial statements of Kommunalkredit pursuant to the Austrian Company Code/Austrian Banking Act, calculated in accordance with CRR, show the following composition and development:

Basis for calculation in EUR 1,000	pursuant to Art. 92 CRR 31/12/2017	pursuant to Art. 92 CRR 31/12/2016
Total risk exposure amount pursuant to Art. 92 CRR	992,393.5	686,130.0
of which credit risk	*874,843.9*	*525,827.5*
of which operational risk	*99,943.4*	*108,947.5*
of which CVA charge	*17,502.1*	*51,247.5*
of which default fund of a qualifying counterparty	*104.2*	*107.5*

Own funds	31/12/2017	31/12/2016
Common equity tier 1 after deductible items (CET 1)	232,963.8	225,500.6
Additional own funds after deductible items	64,195.6	64,832.9
Eligible own funds (tier 1 and tier 2)	**297,159.4**	**290,333.5**
Total capital ratio	29.9%	42.3%
Common equity tier 1 ratio	23.5%	32.9%

Own funds, as shown in the above table, include the 2017 profit for the year of Kommunalkredit Austria AG in accordance with the Austrian Company Code/Austrian Banking Act in the amount of TEUR 18,865.8; the proposed dividend in the amount of TEUR 11,500.0 was deducted from own funds.

INCOME STATEMENT DISCLOSURES OF THE KOMMUNALKREDIT GROUP

46. NET INTEREST INCOME

in EUR 1,000	1/1-31/12/2017	01/01-31/12/2016
Interest income	**157,134.9**	**172,112.2**
Interest income from loans and advances to banks	1,980.2	146.0
Interest income from loans and advances to customers*	79,958.4	82,772.1
Interest income from derivatives	69,069.9	82,557.2
Interest income from assets available for sale	6,001.2	6,518.2
Interest income from other assets	125.2	118.7
Interest expenses	**-121,917.1**	**-135,590.5**
Interest expenses for amounts owed to banks	-1,943.9	-695.3
Interest expenses for amounts owed to customers	-15,199.9	-14,653.7
Interest expenses for derivatives	-57,736.6	-62,947.1
Interest expenses for securitised liabilities	-44,362.2	-54,618.6
Interest expenses for subordinated capital	-2,674.5	-2,675.8
Net interest income	**35,217.8**	**36,521.7**

* resulting from interest income reported under Loans and advances to customers and Assets at fair value through profit or loss

Net interest income amounts to TEUR 35,217.8 (1/1-31/12/2016: TEUR 36,521.7). The significantly increased contribution of new business to net interest income of TEUR 7,922.5 (2016: TEUR 242.8) almost completely offset the reduction of income from the in-force portfolio as a result of scheduled redemptions. Owing to negative interest paid on credit balances with the Austrian National Bank (OeNB) and interest on other lendings from credit institutions, the 2017 interest income was depressed by TEUR 1,428.3 (31/12/2016: TEUR 371.8). The corresponding interest expense is shown in the above table under “Interest expenses for amounts owed to banks”.

Interest income and interest expenses are recognised according to the accruals concept. Kommunalkredit uses derivatives mainly to hedge the risk of interest rate changes and/or currency risks. Interest income and expenses are shown as gross amounts, broken down by incoming and outgoing payments.

Financial instruments not measured at fair value through profit or loss resulted in interest income of TEUR 55,919.5 (1/1-31/12/2016: TEUR 53,538.4) and interest expenses of TEUR 64,180.5 (1/1-31/12/2016: TEUR 72,643.4).

47. LOAN IMPAIRMENT

In 2017, loan impairment losses came to TEUR -300.4 (1/1-31/12/2016: TEUR +64.6) and exclusively comprise the increase of the portfolio allowance according to IAS 39.64. As in the previous reporting period, no specific loan loss provisions and credit defaults were booked in 2017. The non-performing-loan ratio remains at 0.0%.

48. NET FEE AND COMMISSION INCOME

in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
Fee and commission income	**18,135.7**	**17,312.4**
Management of support programmes and consultancy business	15,962.4	16,961.6
Lending business	1,316.0	162.1
Other service business	857.3	188.8
Fee and commission expenses	**-877.4**	**-522.6**
Lending business	-196.0	-33.1
Securities business	-488.2	-357.5
Money and FX trading	-193.1	-132.0
Net fee and commission income	**17,258.3**	**16,789.8**

Net fee and commission income in the amount of TEUR 17,258.3 (1/1-31/12/2016: TEUR 16,789.8) primarily includes revenues of TEUR 15,962.4 (1/1-31/12/2016: TEUR 16,961.6) generated by Kommunalkredit Public Consulting GmbH (KPC) through its management of support programmes and its consultancy business. Fee and commission income from the lending business in the amount of TEUR 1,316.0 (1/1-31/12/2016: TEUR 162.1) primarily includes fees from new lending business as well as management and guarantee fees. Arrangements fees of EUR 9.0m for new business transactions closed in 2017 are booked at constant effective interest over the term of the underlying loans and recognised in net interest income.

Fee and commission expenses included TEUR -196.0 (1/1-31/12/2016: TEUR -33.1) from the lending business, TEUR -488.2 (1/1-31/12/2016: TEUR -357.5) from the securities business and TEUR -193.1 (1/1-31/12/2016: TEUR -132.0) from money and FX trading. All fee and commission income and expenses are recognised according to the accruals concept.

49. NET TRADING AND VALUATION RESULT

The net trading and valuation result of the financial year 2017 was positive at TEUR 3,066.4 (1/1-31/12/2016: TEUR 36,231.5) and comprised the following items:

in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
a) Result from financial instruments measured at fair value	**-197.8**	**-9,719.8**
of which fair value option		
a1) of which loans	*-26,389.9*	*-5,844.3*
a2) of which related interest rate derivatives	*26,192.0*	*-3,875.5*
b) Result from early redemption of own issues and from the placement and measurement of assets	**4,559.3**	**48,119.8**
c) Valuation result from fair-value hedge	**-1,304.4**	**-2,163.2**
c1) of which interest rate derivatives	*50,793.8*	*39,932.7*
c2) of which underlying instruments	*-52,098.2*	*-42,095.9*
d) Foreign currency valuation	**9.4**	**-5.5**
Total	**3,066.4**	**36,231.5**

49.1 Result from financial instruments measured at fair value

Kommunalkredit designates assets as belonging to this category in order to avoid or diminish incongruences arising when gains and losses are not measured or recognised on the same accounting basis (accounting mismatch) and/or when assets are managed, measured and reported to management on a fair value basis. The result from financial instruments measured at fair value in 2017 amounted to TEUR -197.8 (1/1-31/12/2016: TEUR -9,719.8) and included the following components:

- The result from loans and advances to customers and bonds designated as at fair value amounted to TEUR -26,389.9 (1/1-31/12/2016: TEUR -5,844.3), including an effect due to credit spread changes in the amount of TEUR -120.0 (1/1-31/12/2016: TEUR -3,610.0); the cumulative effect from credit spread changes amounts to TEUR -3,620.0 (1/1-31/12/2016: TEUR -3,500.0). Apart from credit spread changes, this earnings component reflects interest-related measurement changes as well as pull-to-part effects of the cumulative positive fair value measurements.
- Interest rate derivatives not part of fair value hedges generated a compensating positive development of TEUR 26,192.0 (1/1-31/12/2016: negative development of TEUR -3,875.5).

49.2 Results realised from the redemption/buyback of own issues and the placement and measurement of assets

Gains realised from the buyback/early redemption of own issues (securitised liabilities) and the closure of the related derivatives amounted to TEUR 6,238.6 in 2017 (1/1-31/12/2016: TEUR 51,120.7). Moreover, this item also comprises the impairment charge on an equity instrument in the amount of TEUR -1,181.0 (1/1-31/12/2016: TEUR 0.0) and other results from the sale and/or measurement of asset portfolios in the amount of TEUR -498.3 (1/1-31/12/2016: TEUR -3,000.9).

49.3 Measurement result from the fair value hedge

The measurement result from the fair value hedge shows the ineffectiveness of the hedging relationships accounted for by Kommunalkredit. For details on hedge accounting and the measurement of effectiveness, see Note 15.

49.4 Result of the held-for-trading portfolio according to IFRS (interest rate derivatives, foreign currency measurement)

It is Kommunalkredit’s business strategy not to engage in any activities with the intention to trade. According to IFRS, the result from the measurement of derivatives, by definition, is to be recognised in the held-for-trading portfolio. However, for Kommunalkredit these are not trading positions, but economic hedges.

According to IFRS definitions, the result of the held-for-trading portfolio amounts to TEUR 26,201.4 (1/1-31/12/2016: TEUR -3,881.0) and includes the following components shown in the above table:

- a2) Interest rate derivatives (trading) in the amount of TEUR 26,192.0 (1/1-31/12/2016: TEUR -3,875.5)
- d) Foreign currency measurement in the amount of TEUR 9.4 (1/1-31/12/2016: TEUR -5.5)

50. GENERAL ADMINISTRATIVE EXPENSES

in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
Personnel expenses	**-38,764.3**	**-31,472.4**
Salaries	-27,163.7	-23,460.3
Statutory social security contributions	-6,329.1	-5,716.6
Voluntary social security contributions	-754.0	-688.0
Expenses for efficiency measures	-2,700.0	0.0
Expenses for pensions and employee benefits	-1,817.6	-1,607.5
Other administrative expenses	**-18,104.0**	**-15,836.2**
Depreciation, amortisation and impairment of	**-1,779.9**	**-2,021.5**
intangible assets	-221.3	-269.6
property, plant and equipment	-1,558.6	-1,751.8
Total	**-58,648.3**	**-49,330.0**

General administrative expenses in the reporting period amounted to TEUR 58,648.3 (1/1-31/12/2016: TEUR 49,330.0).

The increase in personnel expenses to TEUR 38,764.3 (1/1-31/12/2016: TEUR 31,472.4) primarily results from the recruitment of additional personnel for front office units and the establishment of the new branch office in Frankfurt am Main, which was opened at the beginning of 2017. At the same time, the bank implemented an efficiency programme to improve its operational processes, which will result in a reduction of the cost base in 2018. The related expenses, including the commitment to voluntary severance pay, are shown in the above table under “Expenses for efficiency measures”, the major part of which were accounted for in 2017.

Expenses for pensions and employee benefits include TEUR 712.2 (2016: TEUR 671.5) for defined-contribution pension plans (contributions to the pension fund agreed upon through collective bargaining), TEUR 297.4 (2016: TEUR 260.8) in contributions to company pension plans, and TEUR 56.4 (2016: TEUR 0.0) in severance pay.

Other administrative expenses include the following items:

in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
Third-party services	-5,793.7	-5,358.9
Consulting and auditing fees	-1,972.7	-1,895.8
IT	-2,094.1	-2,045.1
Public relations and advertising	-972.7	-1,080.0
External news services	-1,389.4	-1,332.8
Headhunting and personnel development	-435.9	-1,252.8
Rating	-155.0	-208.5
Other administrative expenses	-2,300.4	-2,150.5
Sub-total of other administrative expenses	**-15,113.9**	**-15,324.3**
Strategic initiatives	-2,990.1	-511.8
Total of other administrative expenses	**-18,104.0**	**-15,836.2**

Other administrative expenses increased by TEUR 2,267.8 year on year to TEUR 18,104.0 (2016: TEUR 15,836.2).The total comprises costs of TEUR 2,990.1 for new strategic initiatives (2016: TEUR 511.8), in particular the establishment of the online platform KOMMUNALKREDIT INVEST, which is the first offer for private individuals to invest in Kommunalkredit and significantly broadens the bank's funding options. Corrected for these one-off investments, other administrative expenses were TEUR 210.4 below the previous year's level.

Auditing fees counting towards the reporting period came to a total of TEUR 192.9 (1/1-31/12/2016: TEUR 210.0). The amount includes TEUR 53.1 (1/1-31/12/2016: TEUR 143.4 for the audit of the separate financial statements, TEUR 32.1 (1/1-31/12/2016: TEUR 35.2) for the audit of the consolidated financial statements, and TEUR 107.8 (1/1-31/12/2016: TEUR 31.3) for other audit services. Fees for non-audit services provided by the auditor amounted to TEUR 174.1 in 2017 (1/1-31/12/2016: TEUR 120.0).

51. BANK RESOLUTION FUND

The 2017 contribution to the European Bank Resolution Fund amounted to TEUR 1,699.5. After the release of accruals of TEUR 750.0, the contribution paid depressed earnings by TEUR 949.5 (1/1-31/12/2016: TEUR 2,508.6).

52. OTHER OPERATING RESULT

in EUR 1,000	1/1-31/12/2017	01/01-31/12/2016
Other operating income	**12,531.6**	**11,530.2**
Income from services provided for KA Finanz AG	12,105.8	10,872.9
Other operating income	425.8	657.3
Other operating expenses	**-1,282.8**	**-11,646.1**
Bank stability tax	-675.6	-11,578.6
Other	-607.3	-67.4
Total	**11,248.7**	**-115.9**

Kommunalkredit acts as a service provider for the banking operations of KA Finanz AG. The services to be provided are defined in a service agreement and a service level agreement. In 2017, an amount of TEUR 12,105.8 (1/1-31/12/2016: TEUR 10,872.9) was invoiced to KA Finanz AG for services rendered.

Other operating expenses mainly include the stability tax payable by Austrian banks in the amount of TEUR -675.6 (1/1-31/12/2016: TEUR -11.578.6). In 2016, Kommunalkredit elected to make a non-recurrent special payment of TEUR -7,718.4, which results in a notable reduction of this tax burden from 2017 onwards.

53. TAXES ON INCOME

in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
Current tax expense	-514.4	-390.0
Deferred tax assets	11,517.8	13,936.7
Total	**11,003.4**	**13,546.7**

The current tax expense is calculated on the basis of the taxable profit of the business year at the local tax rate applicable to the Group companies concerned (as in the previous year, all Group companies were subject to the Austrian corporate income tax rate of 25%).

Deferred tax assets in the amount of TEUR 11,517.8 (1/1-31/12/2016: TEUR 13,936.7) result not only from changes in temporary differences, but also from the capitalisation of tax loss carryforwards. Based on the results of tax budgeting, tax loss carryforwards of TEUR 31,394.0 as at 31 December 2017 (31/12/2016: TEUR 21,917.7) were capitalised. Capitalised tax loss carryforwards of TEUR -4,001.6 (1/1-31/12/2016: TEUR -13,768.5) were used in the reporting year. Following the formation of a tax group pursuant to § 9 of the Corporate Income Tax Act with Satere Beteiligungsverwaltungs GmbH as the group parent (for details see Note 22), tax loss carryforwards from periods before the effective date of the group of companies (pre-group losses) can be offset by Kommunalkredit up to the amount of its own profit.

Deferred tax assets do not contain any amounts based on changes in tax rates or new taxes. The following reconciliation table shows the relation between expected and reported taxes on income:

Tax reconciliation table in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
Profit for the year before tax	**7,051.4**	**35,408.7**
Expected tax expense/tax assets in the financial year at the Austrian income tax rate (25%)	-1,762.9	-8,852.2
Decrease of tax expense due to tax-exempt income from associates	40.3	19.5
Decrease of tax expense due to other tax-exempt income	5.6	1.8
Increase of tax expense due to non-deductible items	-489.4	-21.4
Aperiodic tax expense	-256.2	-95.7
Capitalisation of tax loss carryforward	13,477.8	22,885.3
Other	-11.7	-390.7
Taxes on income	**11,003.5**	**13,546.7**

OTHER DISCLOSURES

54. SIGNIFICANT EVENTS AFTER THE BALANCE SHEET DATE

Since the beginning of 2018, Kommunalkredit's online platform for retail clients, KOMMUNALKREDIT INVEST, has been operational in Germany. KOMMUNALKREDIT INVEST takes deposits repayable on demand as well as fixed-term deposits for terms of up to ten years.

In February 2018, KA Finanz AG published a tender for services currently provided by Kommunalkredit. The bank intends to submit an offer for the continuation of such services. A decision by KA Finanz AG is expected by midyear 2018. Should the bank not be awarded with a continuing contract, the service contract with KA Finanz AG will expire in the first half of 2019. In such case the operative capacity will be adjusted during a contractually existing transition period of 12 months.

55. BREAKDOWN OF REVENUES BY REGION

Kommunalkredit operates primarily in the field of municipal and infrastructure-related project business. The bank's activities are concentrated in a single business segment, the results of which are reported regularly to the Executive Board and the Supervisory Board by way of the consolidated financial statements prepared according to IFRS. The disclosures relating to the business segment are presented in the Balance Sheet and the Income Statement of the Group. Reconciliation is therefore not required.

Information on geographic regions for the reporting year, broken down into net interest income and net fee and commission income, is shown in the following table (for additional information on the geographic breakdown of the credit volume, see Note 68.5.4. Economic country risk):

Presentation of revenues by region (registered office of counterparty) 2017 in EUR 1,000	Austria	Europe	Rest of World	Total
Interest and similar income	108,020.9	48,622.7	491.3	157,134.9
Interest and similar expenses	-76,5246	-45,460.8	68.3	-121,917.1
Net interest income	**31,496.3**	**3,161.9**	**559.6**	**35,217.8**
Net fee and commission income	**12,224.7**	**5,033.0**	**0.6**	**17,258.3**

The comparative figures for the period from 1 January 2016 to 31 December 2016 are as follows:

Presentation of revenues by region (registered office of counterparty) 2016 in EUR 1,000	Austria	Europe	Rest of World	Total
Interest and similar income	136,896.9	35,215.3	0.0	172,112.2
Interest and similar expenses	-105,084.8	-30,505.7	0.0	-135,590.5
Net interest income	**31,812.1**	**4,709.6**	**0.0**	**36,521.7**
Net fee and commission income	**13,152.6**	**3,637.2**	**0.0**	**16,789.8**

56. BREAKDOWN BY RESIDUAL MATURITY

Residual maturity is defined as the period between the balance sheet date and the contractual due date of the claim or liability; for partial amounts, residual maturity is shown separately for each part. Interest accruals are recognised under "up to 3 months".

Cash collateral is shown under "repayable on demand" (daily payment terms).

For details on liquidity risk management, see Note 68 (Risk management).

The breakdown of the book values of material asset and liability items by residual maturity as at 31 December 2017 is as follows:

Assets by residual maturity as at 31/12/2017 in EUR 1,000	Repayable on demand	up to 3 months	3 months up to 1 year	1 to 5 years	more than 5 years	Total
Cash and balances with central banks	318,109.1	0.0	0.0	0.0	0.0	**318,109.1**
Loans and advances to banks	101,809.8	10.0	0.0	38,377.8	0.0	**140,197.5**
Loans and advances to customers	97,213.9	95,812.7	102,063.4	836,181.1	960,608.6	**2,091,879.7**
Assets at fair value through profit or loss	0.0	23,356.2	28,816.4	202,318.0	351,240.5	**605,731.1**
Assets available for sale	0.0	3,867.0	107,860.8	1,989.7	97,846.8	**211,564.2**
Investments in associates	0.0	0.0	0.0	0.0	0.0	**0.0**
Other assets	7,193.3	80.6	86.4	727.9	1,282.3	**9,370.4**
Total[1]	**524,326.1**	**123,126.5**	**238,827.0**	**1,079,594.4**	**1,410.978.1**	**3,376,852.1**

Liabilities by residual maturity as at 31/12/2017 in EUR 1,000	Repayable on demand	up to 3 months	3 months up to 1 year	1 to 5 years	more than 5 years	Total
Amounts owed to banks	114,768.3	21,004.5	5,850.2	386,867.4	4,347.8	**532,838.2**
Amounts owed to customers	212,325.1	163,051.0	242,330.9	110,650.9	309,644.1	**1,038,002.0**
Securitised liabilities	0.0	17,743.3	21,853.4	766,617.9	662,367.5	**1,468,582.1**
Subordinated liabilities	0.0	2,527.3	0.0	28,236.2	38,158.7	**68,922.1**
Other liabilities	7,369.7	82.3	7,218.2	3,565.3	748.0	**18,983.5**
Total[1]	**334,463.1**	**204,408.4**	**277,252.7**	**1,295,937.7**	**1,015,266.1**	**3,127,327.9**

[1] The table only shows material asset and liability items; the total therefore does not correspond to the bank's total assets.

Breakdown by residual maturity as at 31 December 2016:

Assets by residual maturity as at 31/12/2016 in EUR 1,000	Repayable on demand	up to 3 months	3 months up to 1 year	1 to 5 years	more than 5 years	Total
Cash and balances with central banks	310,457.4	0.0	0.0	0.0	0.0	**310,457.4**
Loans and advances to banks	101,865.4	0.0	0.0	0.0	0.0	**101,865.4**
Loans and advances to customers	43,070.6	36,467.1	222,527.9	702,502.7	1,134,360.7	**2,138,929.0**
Assets at fair value	0.0	23,905.6	36,472.5	223,915.7	407,322.3	**691,616.0**
Assets available for sale	0.0	18,840.0	10,603.3	113,892.0	3,615.1	**146,950.4**
Investments in associates	0.0	0.0	0.0	0.0	0.0	**0.0**
Other assets	15,083.7	34.7	214.9	717.8	1,459.4	**17,510.6**
Total[1]	**470,477.2**	**79,247.4**	**269,818.6**	**1,041,028.1**	**1,546,757.4**	**3,407,328.8**

Liabilities by residual maturity as at 31/12/2016 in EUR 1,000	Repayable on demand	up to 3 months	3 months up to 1 year	1 to 5 years	more than 5 years	Total
Amounts owed to banks	226,607.0	160,995.7	61,886.6	334,998.0	10,540.5	**795,027.9**
Amounts owed to customers	5,447.3	95,044.9	90,450.2	44,486.3	316,664.3	**552,093.0**
Securitised liabilities	0.0	322,400.9	24,934.3	403,512.2	1,028,318.1	**1,779,165.4**
Subordinated liabilities	0.0	3,100.5	0.0	6,166.6	60,579.7	**69,846.8**
Other liabilities	6,323.1	7,753.6	6,429.7	3,511.6	1,012.4	**25,030.5**
Total[1]	**238,377.4**	**589,295.6**	**183,700.8**	**792,674.7**	**1,417,115.0**	**3,221,163.6**

[1] The table only shows material asset and liability items; the total therefore does not correspond to the bank's total assets.

57. CLASSES OF FINANCIAL INSTRUMENTS

For a definition of the classes of financial instruments, see Note 16.

The following table shows the book values and the fair values of the classes of financial instruments and financial liabilities, as defined by Kommunalkredit, and their reconciliation to the individual balance-sheet items:

Classes: 31/12/2017 in EUR million	Cash and balances with central banks	At fair value through profit or loss: held for trading	At fair value through profit or loss: fair value option	Loans and receivables: Loans and advances to banks	Loans and receivables: Loans and advances to customers	Available for sale	Liabilities at amortised cost	Derivatives designated as hedging instruments	Book value	Fair value
Cash and balances with central banks	318.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	318.1	318.1
Loans and advances to banks	0.0	0.0	0.0	140.2	0.0	0.0	0.0	0.0	140.2	139.8
Loans and advances to customers	0.0	0.0	0.0	0.0	2,091.9	0.0	0.0	0.0	2,091.9	2,195.1
Assets at fair value through profit or loss	0.0	0.0	605.7	0.0	0.0	0.0	0.0	0.0	605.7	605.7
Assets available for sale	0.0	0.0	0.0	0.0	0.0	211.6	0.0	0.0	211.6	211.6
Derivatives	0.0	10.8	0.0	0.0	0.0	0.0	0.0	221.8	232.6	232.6
Amounts owed to banks	0.0	0.0	0.0	0.0	0.0	0.0	532.8	0.0	532.8	532.9
Amounts owed to customers	0.0	0.0	0.0	0.0	0.0	0.0	1,038.0	0.0	1,038.0	997.7
Derivatives	0.0	167.3	0.0	0.0	0.0	0.0	0.0	77.4	244.7	244.7
Securitised liabilities	0.0	0.0	0.0	0.0	0.0	0.0	1,468.6	0.0	1,468.6	1,421.2
Subordinated liabilities	0.0	0.0	0.0	0.0	0.0	0.0	68.9	0.0	68.9	58.4

The previous year's figures are as follows:

Classes 31/12/2016 in EUR million	Cash and balances with central banks	At fair value through profit or loss: held for trading	At fair value through profit or loss: fair value option	Loans and receivables: Loans and advances to banks	Loans and receivables: Loans and advances to customers	Available for sale	Liabilities at amortised cost	Derivatives designated as hedging instruments	Book value	Fair value
Cash and balances with central banks	310.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	310.5	310.5
Loans and advances to banks	0.0	0.0	0.0	101.9	0.0	0.0	0.0	0.0	101.9	101.9
Loans and advances to customers	0.0	0.0	0.0	0.0	2,138.9	0.0	0.0	0.0	2,138.9	2,269.4
Assets at fair value through profit or loss	0.0	0.0	691.6	0.0	0.0	0.0	0.0	0.0	691.6	691.6
Assets available for sale	0.0	0.0	0.0	0.0	0.0	147.0	0.0	0.0	147.0	147.0
Derivatives	0.0	26.5	0.0	0.0	0.0	0.0	0.0	310.7	337.2	337.2
Amounts owed to banks	0.0	0.0	0.0	0.0	0.0	0.0	795.0	0.0	795.0	793.7
Amounts owed to customers	0.0	0.0	0.0	0.0	0.0	0.0	552.1	0.0	552.1	497.0
Derivatives	0.0	170.1	0.0	0.0	0.0	0.0	0.0	93.2	263.3	263.3
Securitised liabilities	0.0	0.0	0.0	0.0	0.0	0.0	1,779.2	0.0	1,779.2	1,658.3
Subordinated liabilities	0.0	0.0	0.0	0.0	0.0	0.0	69.8	0.0	69.8	56.0

The fair values of securities and loans are determined according to the method and hierarchy described in Note 14 in conjunction with Note 67. To determine the fair values of other financial instruments not measured at fair value, maturity-, rating- and instrument-specific measurement parameters, in combination with prevailing measurement methods, are used.

The maximum risk of default by class of financial instruments corresponds to the book values shown in the table. The maximum risk of default of financial guarantees and irrevocable credit commitments corresponds to a nominal value of TEUR 6,291.1 (31/12/2016: TEUR 9,530.9) and TEUR 135,370.9 (31/12/2016: TEUR 39,364.1), respectively.

58. ASSET QUALITY BY CLASS OF FINANCIAL INSTRUMENTS

The asset quality of financial assets that are neither past due nor impaired, broken down by class of financial instruments, can be classified according to the risk structure explained in Note 8. Exposures in risk class 1 are serviced on schedule and are therefore not considered to be at risk of default.

31/12/2017 Book values in EUR 1,000	Risk status Risk class 0	Risk class 1	Risk class 2	Risk class 3
Cash and balances with central banks	318,109.1	0.0	0.0	0.0
Interest rate derivatives (trading)	10,788.8	0.0	0.0	0.0
Fair value option	605,731.1	0.0	0.0	0.0
Loans and advances to banks	140,197.5	0.0	0.0	0.0
Loans and advances to customers	2,070,731.5	21,148.2	0.0	0.0
Available for sale	211,564.2	0.0	0.0	0.0
Derivatives designated as hedging instruments	221,828.0	0.0	0.0	0.0
Total	**3,578,950.3**	**21,148.2**	**0.0**	**0.0**

Other off-balance-sheet obligations in a nominal amount of TEUR 135,370.9 (31/12/2016: TEUR 39,364.1) include credit commitments in the amount of TEUR 1,945.9 (31/12/2016: TEUR 2,144.8) in risk class 1. Contingent liabilities (sureties and guarantees from the lending business) in the amount of TEUR 6,288.6 (31/12/2016: TEUR 9,528.4) and other off-balance-sheet obligations are all in risk class 0.

The figures for the previous year are as follows:

31/12/2016 Book values in EUR 1,000	Risk status Risk class 0	Risk class 1	Risk class 2	Risk class 3
Cash and balances with central banks	310,457.4	0.0	0.0	0.0
Interest rate derivatives (trading)	26,492.8	0.0	0.0	0.0
Fair value option	691,616.0	0.0	0.0	0.0
Loans and advances to banks	112,369.5	0.0	0.0	0.0
Loans and advances to customers	2,124,231.7	21,703.9	0.0	0.0
Available for sale	146,950.4	0.0	0.0	0.0
Derivatives designated as hedging instruments	310,663.6	0.0	0.0	0.0
Total	**3,722,781.4**	**21,703.9**	**0.0**	**0.0**

For further details on the credit risk structure, see Note 68 (Risk management).

59. BOOK VALUE ACCORDING TO IAS 39 MEASUREMENT CATEGORIES

According to IAS 39 measurement categories, the book values of the financial assets and liabilities held by Kommunalkredit are as follows:

in EUR 1,000	31/12/2017	31/12/2016
Assets		
Loans and receivables	2,550,186.3	2,568,762.4
Fair value option	605,731.1	691,616.0
Interest rate derivatives (trading)	232,616.8	337,156.4
Available for sale	211,564.2	146,950.4
in EUR 1,000	**31/12/2017**	**31/12/2016**
Liabilities		
Amortised cost	3,108,344.4	3,221,163.6
Interest rate derivatives (trading)	244,709.4	263,347.5

60. SUBORDINATED ASSETS

As in the previous year, Kommunalkredit had no subordinated assets as at 31 December 2017.

61. ASSETS ASSIGNED AS COLLATERAL

61.1. Collateralised derivatives

As regards collateralised derivatives, a distinction is made between bilateral and cleared derivative contracts.

Pursuant to Regulation (EU) 2016/2251, which entered into force on 1 March 2017, bilateral derivative contracts are subject to a collateralisation requirement. Kommunalkredit complies with all requirements arising in this context. Based on ISDA/CSA arrangements and/or Austrian and German framework contracts/collateral annexes, no other than cash and cash equivalents (cash collateral) were deposited as collateral by Kommunalkredit with counterparties and/or received by Kommunalkredit from counterparties as at 31 December 2017. The positive and negative present values, calculated by counterparty, are offset against one another and the resulting aggregate portfolio present value, calculated by counterparty – taking collateral parameters into account (threshold, minimum transfer amount) – is put up or called.

Kommunalkredit uses the services of the London Clearinghouse (LCH) as the central counterparty via two clearing brokers. Initial and variation margins are exchanged for cleared derivative contracts.

Offsetting of all payment claims from the market values of derivatives and the repayment of collateral is not possible, except in the event of counterparty default. There is no unconditional right of offset.

61.2. Collateralised funding

- Kommunalkredit has assigned securities as collateral for global loans and other funding received from the European Investment Bank in Luxembourg. The collateral taker has the right to realise the collateral only in the event of the debtor's default.

- For covered bonds issued by Kommunalkredit, loans and securities were assigned to a cover pool which can only be drawn on with the approval of a government commissioner.

- For funding obtained through participation in the ECB tender, assets were provided as collateral as at 31 December 2017, which the collateral taker has the right to realise only in the event of the debtor's default.

The following table shows the book values of derivatives and funding received and the corresponding financial collateral, broken down by balance sheet item according to IFRS 7.13A-F. As none of the transactions meet the prerequisites for offsetting according to IAS 32.42, they are shown on the balance sheet in gross amounts.

61.3. Collateral provided for the liability of KA Finanz AG arising from the demerger

As collateral for the liability rising from the demerger for KA Finanz AG, which is liable jointly and severally with Kommunalkredit for the obligations which arose prior to the entry of the demerger in the Companies Register on 26 September 2015 and were transferred to Kommunalkredit, Kommunalkredit issued a covered bond with a nominal value of TEUR 107,000.0 and pledged it to KA Finanz AG. As the covered bond was not placed on the market, it is not recognised as a liability on the balance sheet.

Book values 31/12/2017 in EUR 1,000	Fair value of collateralised derivative	Funding received (-)	Collateral received (-) and provided (+) in the form of financial instruments	Total
Market values of derivatives according to ISDA/CSA arrangements and/or in central clearing	**-11,255.2**		**24,509.3**	**13,254.1**
Derivatives (positive market value)	218,326.6			
Derivatives (negative market value)	-229,581.8			
Loans and advances to banks			87,362.2	
Loans and advances to customers			97,079.0	
Amounts owed to banks			-96,216.0	
Amounts owed to customers			-63,715.8	
European Investment Bank	**0.0**	**-62,209.4**	**68,719.1**	**6,509.7**
Amounts owed to banks		-62,209.4		
Assets available for sale			68,719.1	
Covered issues	**0.0**	**-1,123,636.9**	**1,382,330.5**	**258,693.6**
Securitised liabilities		-1,016,529.4		
Collateral for KA Finanz AG's liability arising from the demerger		-107,107.5		
Loans and advances to customers			792,641.2	
Assets at fair value through profit or loss			516,813.5	
Derivatives (positive market value)			76,662.7	
Derivatives (negative market value)			-3,787.0	
ECB tender	**0.0**	**-312,431.8**	**346,287.3**	**33,855.5**
Amounts owed to banks		-312,431.8		
Loans and advances to customers			295,045.5	
Assets available for sale			51,241.8	
Other	**0.0**	**-25,292.4**	**30,444.8**	**5,152.4**
Amounts owed to banks		-18,929.9		
Securitised liabilities		-6,362.5		
Loans and advances to customers			30,266.5	
Assets at fair value through profit or loss			178.3	
Total	**-11,255.2**	**-1,523,570.5**	**1,852,291.0**	**317,465.4**

The comparative figures as at 31 December 2016 are as follows:

Book values 31/12/2016 in EUR 1,000	Fair value of collateralised derivative	Funding received (-)	Collateral received (-) and provided (+) in the form of financial instruments	Total
Collateralised derivatives	**79,118.7**	**0.0**	**-82,424.1**	**-3,305.4**
Derivatives (positive market value)	314,615.2			
Derivatives (negative market value)	-235,496.5			
Loans and advances to banks			91,030.6	
Loans and advances to customers			43,050.0	
Amounts owed to banks			-216,491.6	
Amounts owed to customers			-13.1	
European Investment Bank	**0.0**	**-64,638.9**	**71,712.6**	**7,073.6**
Amounts owed to banks		-64,638.9		
Assets available for sale			71,712.6	
Covered bond issues	**0.0**	**-1,362,141.7**	**1,487,563.0**	**125,421.3**
Securitised liabilities		-1,254,994.6		
Collateral for KA Finanz AG’s liability arising from the demerger		-107,147.4		
Loans and advances to customers			814,038.7	
Assets at fair value through profit or loss			591,297.8	
Derivatives (positive market value)			95,301.5	
Derivatives (negative market value)			-13,075.0	
ECB tender	**0.0**	**-463,930.0**	**540,248.6**	**76,318.6**
Amounts owed to banks		-463,930.0		
Loans and advances to customers			540,248.6	
Other	**0.0**	**-27,345.4**	**33,273.8**	**5,928.3**
Amounts owed to banks		-20,806.8		
Securitised liabilities		-6,538.6		
Loans and advances to customers			33,075.2	
Assets at fair value through profit or loss			198.5	
Total	**79,118.7**	**-1,918,056.0**	**2,050,373.8**	**211,436.5**

62. CONTINGENT LIABILITIES

Contingent liabilities comprise sureties and guarantees from the lending business in a nominal amount of TEUR 6,291.1 (31/12/2016: TEUR 9,530.9). The residual maturities are as follows:

Residual maturity in EUR 1,000	31/12/2017	31/12/2016
Up to 1 year	136.1	737.1
1 to 5 years	4,392.1	7,030.8
More than 5 years	1,762.9	1,762.9
Total	**6,291.1**	**9,530.9**

A future outflow of funds from contingent liabilities is considered unlikely.

63. OTHER OFF-BALANCE-SHEET LIABILITIES

As at 31 December 2017, the nominal value of loan commitments and unused lines was TEUR 135,370.9 (31/12/2016: TEUR 39,364.1); moreover, a payment obligation for an investment in equity instruments amounted to TEUR 2,150.0 (TEUR 3,175.0). The residual maturities are as follows:

Residual maturity in EUR 1,000	31/12/2017	31/12/2016
Up to 1 year	34,890.6	18,366.8
1 to 5 years	93,451.2	13,807.7
More than 5 years	7,029.1	7,189.6
Total	**135,370.9**	**39,364.1**

Moreover, Kommunalkredit holds in trust and manages in its own name financial instruments with a nominal value of TEUR 435,246.0 (31/12/2016: TEUR 218,001.3) at third parties' risk and cost.

64. DERIVATIVE FINANCIAL INSTRUMENTS

Kommunalkredit uses derivatives primarily to hedge interest rate and/or currency risks. The structure of open derivative financial transactions is as follows:

31/12/2017 in EUR 1,000	Nominal as at 31/12/2017 Residual maturity up to 1 year	1-5 years	more than 5 years	Nominal Total 2017	Positive fair value	Negative fair value
Interest-related transactions	**170,056.1**	**1,085,242.3**	**1,816,428.1**	**3,071,726.5**	**231,392.0**	**-205,016.7**
OTC products						
Interest rate swaps – Trading*	30,000.0	230,282.1	611,477.2	871,759.3	10,487.1	-130,603.8
Interest rate swaps – Fair value hedge	140,056.1	854,960.2	1,204,951.0	2,199,967.2	220,905.0	-74,412.9
Currency-related transactions	**740,221.8**	**27,424.0**	**0.0**	**767,645.8**	**1,224.8**	**-39,692.6**
OTC products						
FX forwards	740,221.8	0.0	0.0	740,221.8	301.7	-36,701.5
Interest rate and currency swaps – Fair value hedge	0.0	27,424.0	0.0	27,424.0	923.1	-2,991.2
Total	**910,277.9**	**1,112,666.3**	**1,816,428.1**	**3,839,372.3**	**232,616.8**	**-244,709.4**

* Interest rate swaps – Trading are in economic hedges outside the scope of hedge accounting according to IAS 39. The measurement effects from changes in the fair value of these derivatives are booked against the measurement results from financial instruments measured at fair value (see Note 49 Net trading and valuation result).

31/12/2016 in EUR 1,000	Nominal as at 31/12/2016 Residual maturity up to 1 year	1-5 years	more than 5 years	Nominal Total 2015	Positive fair value	Negative fair value
Interest-related transactions	**366,334.8**	**758,857.4**	**2,175,556.7**	**3,300,748.9**	**318,641.8**	**-248,296.5**
OTC products						
Interest rate swaps – Trading*	25,000.0	208,071.3	683,697.5	916,768.8	8,833.8	-156,512.6
Interest rate swaps – Fair value hedge	341,334.8	550,786.1	1,441,859.2	2,383,980.1	309,808.0	-91,783.9
Currency-related transactions	**1,067,469.6**	**25,598.8**	**0.0**	**1,093,068.5**	**18,514.6**	**-15,051.0**
OTC products						
FX forwards	1,067,469.6	0.0	0.0	1,067,469.6	17,659.0	-13,597.9
Interest rate and currency swaps – Fair value hedge	0.0	25,598.8	0.0	25,598.8	855.6	-1,453.1
Total	**1,433,804.4**	**784,456.2**	**2,175,556.7**	**4,393,817.4**	**337,156.4**	**-263,347.5**

* Interest rate swaps – Trading are in economic hedges outside the scope of hedge accounting according to IAS 39. The measurement effects from changes in the fair value of these derivatives are booked against the measurement results from financial instruments measured at fair value (see Note 49 Net trading and valuation result).

Compared to 31 December 2016, the nominal amount of open derivative financial transactions decreased by TEUR 554,445.1 to TEUR 3,839,372.3. Including all positions, the negative fair value amounts to TEUR 12,092.6 (31/12/2016: positive fair value of TEUR 73,808.9), mostly collateralised through cash and cash equivalents according to ISDA-/CSA arrangements. Moreover, there are options embedded in loans and/or own issues, which are fully hedged through options embedded in derivatives. Given the fact that the options are closely associated with their host contracts, they are recognised and measured together with the underlying transactions and not shown in the above table. The negative fair values of these options embedded in loans and own issues amount to TEUR 36,740.9 (31/12/2016: TEUR 8,012.2).

Derivatives with positive fair values in the amount of TEUR 31,329.7 (31/12/2016: TEUR 59,082.7) will fall due within one year, TEUR 42,342.7 (31/12/2016: TEUR 39,288.3) in one to five years, and TEUR 158,944.5 (31/12/2016: TEUR 238,785.4) in more than five years. Derivatives with negative fair values in the amount of TEUR 63,787.4 (31/12/2016: TEUR 36,216.0) will fall due within one year, TEUR 41,557.2 (31/12/2016: TEUR 36,111.7) in one to five years, and TEUR 139,364.9 (31/12/2016: TEUR 191,019.8) in more than five years.

65. BOOK VALUES OF FINANCIAL INSTRUMENTS IN HEDGE ACCOUNTING

Financial instruments the interest rate risk of which is hedged through derivative financial instruments are recognised as fair value hedges. The book values of these underlying transactions are as follows:

in EUR 1,000	31/12/2017	31/12/2016
Assets		
Loans and advances to customer – Fair value hedges	519,688.7	523,342.6
Asset available for sale – Fair value hedges	208,733.8	132,485.4
Liabilities		
Amounts owed to customer – Fair value hedges	300,922.9	312,598.1
Securitised liabilities – Fair value hedges	1,383,057.7	1,697,309.3
Subordinated liabilities – Fair value hedges	45,845.8	46,221.2

66. SUPPLEMENTARY DISCLOSURES PURSUANT TO § 59A AND § 64 OF THE AUSTRIAN BANKING ACT

As at 31 December 2017, neither derivatives nor securities were allocated to the trading book.

Assets denominated in foreign currencies in the amount of EUR 183,080,415.56 (31/12/2016: EUR 160,939,182.25) were shown on the balance sheet. Liabilities denominated in foreign currencies as at 31 December 2017 amounted to EUR 715,245,585.68 (31/12/2016: EUR 1,110,043,793.84). Open currency positions are closed through corresponding swap contracts. As Kommunalkredit's open foreign currency position is continuously monitored and strictly limited, there are no material currency risks.

The return on assets, calculated as the profit for the year after tax divided by total assets as at balance sheet date, stands at 0.49% (2016: 1.29%).

67. DISCLOSURES RELATING TO FAIR VALUE MEASUREMENT (FAIR VALUE HIERARCHY)

In general, the methods used to measure the fair value can be classified in three categories:

- **Level 1**: Quoted prices are available in an active market for identical financial instruments. For this level of the hierarchy, Kommunalkredit refers to bid quotes for assets from Bloomberg and Reuters.

- **Level 2**: The inputs for measurement are observable in the market. This category includes the following pricing methods:
  - Pricing on the basis of comparable securities
  - Pricing on the basis of market-derived spreads (benchmark spreads)

- **Level 3**: Inputs cannot be observed in the market. This category includes, above all, prices based mainly on expert estimates and/or non-observable data. Level 3 financial instruments are measured by means of an internal model based on the net-present-value method. The cash flows are discounted on the basis of current yield curves with due consideration given to credit spreads. Owing to the specific modelling features, project finance transactions are all allocated to level 3.

67.1. Financial instruments recognised at fair value

The following table shows the breakdown of financial instruments recognised at fair value by class of financial instruments according to the fair value hierarchy:

Book values for financial instruments recognised at fair value in EUR 1,000	31/12/2017		
	Level 1	Level 2	Level 3
Available for sale	208,733.8	0.0	0.0
At fair value through profit or loss – Fair value option	0.0	605,731.1	0.0
At fair value through profit or loss – Held for trading (from assets-side items)	0.0	10,788.8	0.0
At fair value through profit or loss – Held for trading (from liability-side items)	0.0	-167,305.3	0.0
Derivatives designated as hedging instruments (from asset-side items)	0.0	221,828.0	0.0
Derivatives designated as hedging instruments (from liability-side items)	0.0	-77,404.1	0.0

The comparative values of the previous year are as follows:

Book values for financial instruments recognised at fair value in EUR 1,000	31/12/2016		
	Level 1	Level 2	Level 3
Available for sale	143,335.3	0.0	0.0
At fair value through profit or loss – Fair value option	0.0	691,616.0	0.0
At fair value through profit or loss – Held for trading (from asset-side items)	0.0	26,492.8	0.0
At fair value through profit or loss – Held for trading (from liability-side items)	0.0	-170,110.5	0.0
Derivatives designated as hedging instruments (from asset-side items)	0.0	310,663.6	0.0
Derivatives designated as hedging instruments (from liability-side items)	0.0	-93,237.0	0.0

No migrations of financial instruments measured at fair value between the levels described above were recording in the period under review.

67.2. Financial instruments not recognised at fair value

The following table shows the breakdown of financial instruments not recognised at fair value by class of financial instruments:

Fair values of financial instruments not recognised at fair value in EUR 1,000	31/12/2017		
	Level 1	Level 2	Level 3
Loans and receivables: Loans and advances to banks	0.0	122,032.1	17,730.6
Loans and receivables: Loans and advances to customers	0.0	1,656,979.4	538,125.6
Liabilities at amortised cost	0.0	-3,010,250.9	0.0

The comparative values of the previous year are as follows:

Fair values of financial instruments not recognised at fair value in EUR 1,000	31/12/2016		
	Level 1	Level 2	Level 3
Loans and receivables: Loans and advances to banks	0.0	101,865.4	0.0
Loans and receivables: Loans and advances to customers	0.0	2,269,444.3	0.0
Liabilities at amortised cost	0.0	-3,005,073.5	0.0

In the reporting year 2017, financial instruments not measured at fair value reported under “Loans and receivables: Loans and advances to customers” with a book value of TEUR 238,545.9 as at 31 December 2017 (corresponding book value as at 31/12/2016: TEUR 268,913.4) were reclassified from level 2 to level 3. The level 3 portfolio in the amount of TEUR 556,856.2 mainly results from new business. Given the fact that no parameters observable in the market (e.g. benchmark spreads) are available for such complex financial instruments, these financial instruments were allocated to level 3. There were no migrations from level 2 to level 3 in 2017, nor were there any migrations from level 2 to level 1 or vice versa.

68. RISK MANAGEMENT

68.1. Risk management strategies and procedures

The instruments used by Kommunalkredit for the complete identification of the risk drivers of the business model are risk assessments and a risk map. Within the framework of risk assessment, the main types of risk for the bank are identified through a structured analytical process. Based on the results of the assessment, a risk map is drawn up for the bank as a whole, which contains a definition of risks, broken down by risk type, and assesses the individual risks in terms of significance, risk transparency, control frequency and limitation. The risk map serves to establish a uniform understanding of the risk concept and a uniform view of risk priorities, and to review the system for completeness and identify potential control gaps. The types of risk covered are those which are classified as highly relevant, but are characterised by low risk transparency and a low control frequency and are therefore given top priority in respect of further development needs. This analysis is performed annually.

Within the framework of the risk strategy for the main types of risk, the Executive Board specifies the principles for their adequate management and limitation. For each main type of risk and each field of business, the economic risk is limited in accordance with the risk-bearing capacity (ICAAP – Internal Capital Adequacy Assessment Process and/or ILAAP – Internal Liquidity Adequacy Assessment Process) and the risk appetite of the bank. Monthly reviews are performed to check the level of utilisation of the risk budget, as well as the risk appetite, for the entire bank and to verify that it is not overrun. Counterparty limits as well as the operational risk limits for the open FX position are reviewed on a daily basis. Kommunalkredit's business operations do not include any trading activities.

Kommunalkredit has a trading book, but its use is strictly limited. The transactions exclusively are risk-free through-trading activities within the framework of the provision of customer services. Subject to this limited use, Kommunalkredit does not engage in any activities with the intention to trade or any other activities resulting in open positions in the trading book.

68.2. Organisational structure of risk management and risk monitoring

The overall responsibility for ICAAP lies with the Executive Board. The risk-policy principles and the risk strategy are derived from Kommunalkredit's business-policy strategy. The Executive Board also decides on the risk management procedures to be applied and regularly informs the Supervisory Board and/or its committees (above all the Risk Committee, the Audit Committee and the Credit Committee) on Kommunalkredit's risk position.

Kommunalkredit has established an organisational structure for risk management, which clearly defines and sets out the tasks, competences and responsibilities within the framework of the risk management process. Risk-taking organisational units (front office) are clearly separated from organisational units in charge of the monitoring and communication of risks (back office) at all levels up to the Executive Board.

The Chief Risk Officer (CRO) is a member of the Executive Board. The function receives technical and operational support from Risk Controlling and Credit Risk Management. Together, these functions independently perform the tasks of a risk management pursuant to § 39 (5) of the Austrian Banking Act and report directly to Kommunalkredit's Executive Board.

Thus, the organisational structure fully meets the regulatory requirement of separation between front-office and back-office functions.

Pursuant to § 39d of the Austrian Banking Act, a Risk Committee of the Supervisory Board has been set up. The committee's mandate includes, in particular, advising the management on the current and future risk appetite and risk strategy of the bank, monitoring the implementation of this risk strategy in connection with the management, monitoring and limitation of risks, and monitoring the capital position and the liquidity position of the bank. Besides the reports submitted by the Risk Committee, the Supervisory Board regularly receives information on the risk position of the bank through comprehensive quarterly risk reports and a monthly key data sheet showing the development of the most important capital, earnings and risk indicators.

Risks are managed and monitored by the Risk Management Committee (RMC), the Asset-Liability Committee (ALCO) and the Credit Committee.

The Risk Management Committee (RMC) constitutes the central element of the comprehensive risk management process, providing information to the Executive Board on the overall risk position of the bank on a monthly basis. In organisational terms, Risk Controlling is in charge of this committee. The RMC is responsible for the establishment of guidelines for the implementation of the risk strategy and is in charge of limit setting (except country and counterparty limits) and limit monitoring by type of risk.

The weekly Asset-Liability Committee (ALCO) supports the operational management of market and liquidity risks. In organisational terms, the Market Division is in charge of this committee. At its meetings, the committee evaluates the market situation, monitors the limits and discusses the management of interest rate and liquidity risks. In addition, a detailed daily liquidity monitoring process is in place.

The weekly Credit Committee (CC) meeting is the central element of the credit approval process and the continuous portfolio and single-name review process. In organisational terms, Credit Risk is responsible for this committee (analysis and assessment of single-name risks, casting of a second vote on credit approval and/or review, management of single-name risks and/or other risks, work-out cases, qualitative portfolio analyses and rating).

Risk Controlling is responsible for the quantification of risks and the aggregate risk cover as well as for the performance of stress tests.

The objective of asset and liability management is to optimise the use of capital resources in terms of risk and return within the framework of the bank's risk appetite and risk-bearing capacity.

The strategies, methods, reporting rules and organisational responsibilities for the management of risks are documented in writing in the ICAAP manual, in risk management manuals for each type of risk and in organisational guidelines, which can be downloaded via the Intranet in their current versions at any time by all staff members concerned.

The following types of risk were identified up to the balance sheet date and are continuously monitored at Kommunalkredit:

- **Credit risk**
  Default and counterparty risk
  Replacement risk in the event of counterparty default
  Rating migration risk
  Investment risk
  Country and/or transfer risk
  Settlement risk
  Securitisation risk
  Cluster risk
  Concentration risk

- **Liquidity risk**
  Structural liquidity risk
  Funding risk
  Market liquidity risk

- **Market risk**
  Interest rate risk – banking book
  Interest rate risk – trading book
  Currency risk
  Commodity risk
  Credit spread risk
  Basis spread risk
  Option price risk
  OIS risk

- **Operational risk**
  Risks from human failure, processes, systems and external risks
  Legal risk
  Risk from service level agreement (SLA) with KA Finanz AG
  ICT risk

- **Funding risk**
  BCVA risk*
  Replacement risk through rating trigger
  ** comprises CVA risk and DVA risk and is allocated in its entirety to the funding risk*

- **Other risks**
  Strategic risk
  Risk from demerger liability
  Equity risk
  Reputational risk
  Business risk
  Excessive debt risk
  Risk of money laundering and terrorism financing
  Systemic risk from a financial institution
  Macroeconomic risk
  Placement and syndication risk

A formalised and structured approval and implementation procedure has been set up for the introduction of new fields of business, new markets or new products, ensuring that these are adequately reflected in all areas of settlement, risk management and reporting, accounting and financial reporting.

68.3. Risk-policy guidelines for risk management

The guidelines followed at Kommunalkredit are based on the following risk management principles:

- The limitation of risks at Kommunalkredit is commensurate with the bank's earning strength and its equity base.
- Kommunalkredit supports a risk culture characterised by a deliberate management of risks in day-to-day business, observance of the agreed risk appetite and the promotion of open dialogue on risk-related issues at all levels.
- The expertise of Kommunalkredit staff and the systems in place must correspond to the complexity of the business model and have to be developed together with the core fields of business.
- In terms of organisational structure, a clear separation between risk-taking on the one hand and risk calculation and/or risk management on the other hand is essential. Conflicts of interest for staff members are avoided through a clear separation of the different fields of activity.
- Risk management is an integral component of the business process and is based on recognised methods of risk measurement, monitoring and control. For credit and market risks, this principle is applied on an economic basis (value-at-risk approach).
- All measurable risks are subject to a limit structure; regular monitoring of the observance of limits on the basis of transparent and uniform principles is obligatory. An escalation process applies in the event of limit breaches. A capital buffer is kept for risks that have been identified but are not/not yet sufficiently measurable.
- The risk measurement results have to be subjected to regular stress testing and taken into account in determining the risk-bearing capacity of the credit institution. The results of stress testing have to be related to a limit and/or a hedging target.

- Kommunalkredit's system of risk management provides for comprehensive, regular and standardised risk reporting, with reports on the risk position of Kommunalkredit being produced at least once a month and, if necessary, supplemented by ad-hoc risk reports.
- An integrated IT infrastructure, as a prerequisite for the systematic reduction of risks from interfaces and data inconsistencies and as a basis for efficient reporting and data processing, constitutes an essential organisational and risk-policy objective.
- Core areas of the banking business and important control functions are not outsourced, unless an adequate level of know-how and experience is maintained within the bank.

68.4. Securing minimum capital adequacy

ICAAP (Internal Capital Adequacy Assessment Process) and ILAAP (Internal Liquidity Adequacy Assessment Process) are core elements of Pillar 2 of the Basel Accord and comprise all procedures and measures applied by a bank to ensure the appropriate identification, measurement and limitation of risks, a level of capitalisation in line with the risk profile of the business model, and the use and continuous further development of suitable risk management systems.

For the main types of risk (in particular: liquidity risk, credit default risk, market risk and syndication risk), the economic capital required to cover the risk is calculated according to recognised internal bank management procedures. In addition, a risk buffer is provided to cover risks that cannot be adequately quantified (in particular: operational risk, reputational risk, legal risks and other risks) as well as potential model inaccuracies. The economic perspective serves to secure adequate long-term capitalisation of the bank.

Kommunalkredit uses the method of risk-bearing-capacity analysis for the quantitative assessment of its capital adequacy, by which the economic risks are compared with the risk coverage potential. Depending on the hedging target pursued, two economic control loops are applied:

- **Liquidation perspective**
  (economic control loop based on the principle of creditor protection)

  Target: The main focus is on the protection of creditors and on securing a level of capitalisation to ensure that, in the event of liquidation of the company, all lenders can be satisfied with a defined probability.

  Economic capital requirements (internal risk measurement) are compared with the company's own funds, adjusted for hidden burdens and reserves. The aggregate risk cover is determined on the basis of its present value ("full fair value" approach) and is therefore not subject to accounting and measurement rules. A confidence level of 99.95% is used in determining the economic risk.

  Risk status: As at 31 December 2017, the economic risks correspond to 26.3% (31/12/2016: 19.9%) of the aggregate risk cover, the **risk buffer** being **73.7%** (31/12/2016: 80.1%).

- **Going concern perspective**
  (economic control loop based on the going-concern principle)

  Target: If the risks materialise, the survival of the bank as a going concern without additional equity is to be ensured with a defined degree of probability. The defined level of protection from risk under the going-concern perspective is a minimum tier 1 ratio of 13%.

All risks impacting on profit and loss must be covered by the budgeted annual result, realisable reserves and the “free tier 1” capital. Free tier 1 is the tier 1 portion over and above the capital required to secure a tier 1 ratio of 13%. The aggregate risk cover is broken down into primary and secondary coverage potential, always considering possible realisation and external effects; early warning levels have been introduced. A confidence level of 95% is used in determining the economic risk.

Risk status: As at 31 December 2017, the economic risks correspond to 43.1% (31/12/2016: 32.2%) of the aggregate risk cover, the **risk buffer** being **56.9%** (31/12/2016: 67.8%).

Additionally, stress tests are performed regularly to test the robustness of the business model and to ensure capital adequacy. For this purpose, two different economic scenarios (general recession scenario and portfolio-specific stress) are defined and their impact on the bank’s risk-bearing capacity is quantified. In addition to the stressed risk-bearing capacity, a stressed three-year budget is drawn up for each scenario in order to test the stability of the business model over time. Besides the macroeconomic stress tests, reverse stress tests are performed. These are intended to show the extent to which parameters and risks can be stressed before regulatory or internal minimum requirements can no longer be met.

68.5. Credit risk management

Credit risk is the risk of financial losses arising from a counterparty not meeting its contractual payment obligations.

Personal forms of collateral (sureties and guarantees) play an important role in securing credit exposures. If personal collateral is available, the exposure can be counted towards the collateral giver, depending on the assessment of the risk, and included in the portfolio model and the limit system. Financial collateral include netting arrangements and cash collateral that reduce the counterparty risk. Financial collateral received reduces the existing exposure.

Based on the current CRR standardised approach for all classes of receivables, Kommunalkredit primarily uses external ratings. If no external ratings are available, ratings are derived from internal scoring and/or rating models for internal risk control.

Every active customer is assigned an external or internal rating, which is updated at least once a year. Thus, assets on the banking book and off-balance-sheet transactions can be classified fully according to probability of default and collateralisation. On the basis of an internal rating scale (master scale), the probabilities of default are grouped in categories, to which external ratings can be assigned. To ensure a uniform system of determining the probabilities of default, all internal and external rating procedures and/or ratings have to be calibrated against the master scale. The discriminatory power of the rating procedures and their ability to forecast defaults are checked regularly and adjusted, if necessary.

68.5.1. Unexpected loss

To quantify the unexpected loss, monthly credit VaR calculations are performed to manage and limit the risk and to determine the economic capital required within the framework of risk-bearing-capacity analyses. Kommunalkredit uses a default model based on the CreditRisk+ approach to quantify the risk of unexpected default for credit risks. To calculate the credit VaR, rating-dependent one-year probabilities of default (PD) as well as regional and sector-specific loss ratios (LGD) are used. These parameters are reviewed and updated at least once a year and documented in a validation report.

From the **liquidation perspective**, the potential unexpected loss from credit defaults for a holding period of one year as at 31 December 2017 amounted to 5.8% (31/12/2016: 4.3%) relative to the economic aggregate risk cover.

From the **going-concern perspective**, the potential unexpected loss from credit defaults for a holding period of one year as at 31 December 2017 amounted to 14.6% (31/12/2016: 4.2%) relative to the economic aggregate risk cover.

The model used is based on statistical methods and assumptions. It should be pointed out, however, that statistically well-founded conclusions drawn from the past do not always apply to future developments. To take account of this fact, the model calculations are supplemented by additional, event-triggered analyses and regular stress tests, and adequate risk buffers are maintained.

68.5.2. Breakdown by rating

The breakdown of credit exposure by rating shows that the exposure is concentrated in the top rating categories: as at 31 December 2017, 46.4% (31/12/2016: 60.8%) of the exposure was rated “AAA”/“AA”, 89.4% was rated investment grade. Overall, the Kommunalkredit portfolio has a high asset quality; the exposure-weighted average rating of the total exposure is “A” (according to Standard & Poor’s rating scale).

Breakdown of exposure* by rating 31/12/2017 in EUR million	Exposure	Proportion	of which securities	of which guarantees	of which loans
AAA	17.9	0.6%	0.0	0.0	17.9
AA	1,337.2	45.7%	93.9	0.0	1,242.7
A	461.9	15.8%	46.6	0.0	348.1
BBB	795.3	27.2%	145.0	6.0	599.2
BB	249.7	8.5%	0.0	0.0	249.7
B	61.1	2.1%	0.0	0.0	61.1
CCC	0.0	0.0%	0.0	0.0	0.0
D	0.0	0.0%	0.0	0.0	0.0
not rated	0.0	0.0%	0.0	0.0	0.0
Total	**2,923.3**	**100%**	**285.4**	**6.0**	**2,518.8**

* Breakdown of exposure according to S&P rating scale

Breakdown of exposure* by rating 31/12/2016 in EUR million	Exposure	Proportion	of which securities	of which guarantees	of which loans
AAA	48.2	1.7 %	0.0	0.0	48.2
AA	1,694.6	59.1 %	96.3	0.0	1,595.5
A	693.3	24.2 %	108.1	0.0	513.2
BBB	392.0	13.7 %	10.8	9.5	326.3
BB	24.9	0.9 %	0.0	0.0	24.9
B	15.4	0.5 %	0.0	0.0	15.4
CCC	0.0	0.0 %	0.0	0.0	0.0
D	0.0	0.0 %	0.0	0.0	0.0
not rated	0.0	0.0 %	0.0	0.0	0.0
Total	**2,868.5**	**100.0 %**	**215.1**	**9.5**	**2,523.5**

* Breakdown of exposure according to S&P rating scale

68.5.3. Concentration risk

Risk concentrations are taken into account in the process of loan origination, monitored in the course of the monthly credit risk reports to the RMC, and shown in reports to the Credit Committee and the Supervisory Board. The total portfolio is broken down according to different parameters (breakdown by country, region, top 20/100 groups of related customers, rating, sector); limits are set by top risk drivers, sectors and geographic regions. In addition, risk concentrations in individual sub-portfolios are identified by Credit Risk Management, which performs sub-portfolio analyses. Portfolio analyses comprise correlating regional and/or sectorial risks or risk concentrations and permit the early detection, limitation and management of risk portfolios under current and future conditions. Depending on the risk assessment, reviews are performed at different intervals, but at least once a year. Event-triggered portfolio reviews may also be required on an ad-hoc basis and between the scheduled intervals.

The exposure to the top-20 “group of related customers” comprises an exposure of EUR 0.7bn (EUR 1.1bn) to the Republic of Austria and the Austrian provinces, accounting for 44.2% (31/12/2016: 55.1%) of the total exposure. It includes broadly diversified mortgage loans in a total amount of EUR 151.4m (31/12/2016: EUR 156.0m) that are guaranteed by the Austrian provinces concerned. Excluding Austria and the Austrian provinces, the exposure to the top-20 “group of related customers” comprises 25.3% (31/12/2016: 21.8%) of the total exposure.

68.5.4. Economic country risk

Credit exposures are reported for the purpose of internal risk management on the basis of the economic country risk. Kommunalkredit’s country risk is reported monthly to the RCM and at least once a year to the Credit Committee of the Supervisory Board. For each country, information on the country rating, exposure by product type, expected and unexpected loss, and limit utilisation is monitored.

Geographically, most of the exposure is accounted for by EU Member States (EU, incl. Austria, 98.2%). The exposure to non-EU Europe, i.e. 0.3% (31/12/2016: 0.4%) of the total exposure, is accounted for entirely by Switzerland. As at 31 December 2017, Kommunalkredit had no exposure to Greece and Ukraine.

Breakdown of exposure by region 31/12/2017 in EUR million	**Exposure**	**Proportion**	**of which securities**	**of which guarantees**	**of which loans**
Austria	1,826.2	62.5%	79.5	1.5	1,744.0
EU-28 (European Union excl. Austria)	1,044.0	35.7%	193.5	4.5	739.5
of which EU-19 (euro area excl. Austria)	564.2	19.3%	80.4	4.5	423.2
Non-EU Europe	9.0	0.3%	0.0	0.0	4.3
Other	44.1	1.5%	12.4	0.0	31.1
Total	**2,923.3**	**100.0%**	**285.4**	**6.0**	**2,518.8**

Breakdown of exposure by region 31/12/2016 in EUR million	**Exposure**	**Proportion**	**of which securities**	**of which guarantees**	**of which loans**
Austria	2,256.6	79.0 %	96.3	9.1	2,137.7
EU-28 (European Union excl. Austria)	589.7	20.6 %	118.9	0.4	375.4
of which EU-18 (euro area excl. Austria)	*379.7*	*13.2 %*	*10.8*	*0.4*	*297.8*
Non-EU Europe	11.5	0.4 %	0.0	0.0	10.3
Other	1.7	0.1 %	0.0	0.0	0.0
Total	**2,868.5**	**100.0 %**	**215.1**	**9.5**	**2,523.5**

<u>Exposure to sovereigns and territorial authorities as at 31 December 2017</u>

Direct exposures to sovereigns and territorial authorities as well as exposures guaranteed by sovereigns in the countries of the euro area (EU-19) are broken down as follows:

31/12/2017 in EUR million	Exposure	of which sovereigns	of which territorial authorities	of which government-guaranteed
Austria	1,346.1	0.0	1,346.1	0.0
Germany	25.1	0.0	7.2	17.8
Ireland	10.2	10.2	0.0	0.0
Slovakia	10.6	10.6	0.0	0.0
Slovenia	15.7	15.7	0.0	0.0
Italy	10.3	10.3	0.0	0.0
Lithuania	10.2	10.2	0.0	0.0
Spain	21.3	16.0	5.4	0.0

The comparative values of the previous year are as follows:

31/12/2016 in EUR million	Exposure	of which sovereigns	of which territorial authorities	of which government-guaranteed
Austria	1,671.2	0.0	1,671.2	0.0
Germany	56.6	0.0	36.8	19.8
Ireland	0.0	0.0	0.0	0.0
Slovakia	0.0	0.0	0.0	0.0
Slovenia	0.0	0.0	0.0	0.0
Italy	0.0	0.0	0.0	0.0
Lithuania	0.0	0.0	0.0	0.0
Spain	10.8	10.8	0.0	0.0

Except for Austria and Germany, these exposures concern, in particular, securities held for liquidity control.

<u>Exposure to Austrian provinces as at 31 December 2017</u>

Of Kommunalkredit’s total exposure to Austria in a volume of EUR 1,826.2m (31/12/2016: EUR 2,265.6m), the following exposures are to Austrian provinces and/or provincial entities guaranteed by provincial governments:

31/12/2017 in EUR million	Direct exposure	Exposure guaranteed by provincial government	Total exposure
Province of Upper Austria	3.4	95.8	99.2
Province of Lower Austria	33.7	94.1	127.8
Province of Carinthia	0.0	127.1	127.1
Province of Styria	0.0	49.8	49.8
Province of Burgenland	0.0	99.5	99.5
City of Vienna	16.8	0.0	16.8
Total	**53.9**	**466.3**	**520.2**

The comparative values of the previous year are as follows:

31/12/2016 in EUR million	Direct exposure	Exposure guaranteed by provincial government	Total exposure
Province of Upper Austria	7.3	237.1	244.4
Province of Lower Austria	33.8	122.3	156.1
Province of Carinthia	0.0	147.7	147.7
Province of Styria	0.0	114.1	114.1
Province of Burgenland	0.0	101.9	101.9
City of Vienna	20.7	0.0	20.7
Total	**61.8**	**723.1**	**784.9**

In addition to the exposures listed in the above table, Kommunalkredit holds housing loans of Austrian provinces secured by mortgages in a total volume of EUR 151.4m (31/12/2016: EUR 155.6m), which are guaranteed by the provinces concerned (Burgenland EUR 97.1m (31/12/2016: EUR 101.4m); Upper Austria EUR 54.3m (31/12/2016: EUR 54.2m)).

Portfolio quality

Given the good ratings (weighted average rating of the total portfolio "A") and the degree of diversification, the portfolio quality is sound. This is also reflected in the non-performing-loan ratio of 0.00% as at 31 December 2017 (31/12/2016: 0.0%). Kommunalkredit had no financial assets (receivables) on its books that were more than 90 days past due, nor any substantial payment arrears of between 0 and 90 days.

68.5.5. Loan loss provisions

The portfolio is reviewed regularly for objective indications of impairments of customer exposures or exposures to groups of related customers. Assessments of impairment are performed in the course of the annual rating updates, the annual rating review or on an event-triggered basis. Impairments to be booked for defaulting loans are determined by Risk Management, subject to approval by the Executive Board.

Counterparties with increased credit risk

A multi-stage risk control process is applied to identify, monitor and manage counterparties with increased credit risks; all exposures/counterparties are classified in four risk classes.

- Risk class 0: Regular business
- Risk class 1: Intensive management / performing
- Risk class 2: Workout / restructuring
- Risk class 3: Workout / resolution

As at 31 December 2017, the exposure in risk class 1 (intensive management/performing) amounted to EUR 23.4m (31/12/2016: EUR 24.1m). None of Kommunalkredit's exposures are classified as risk classes 2 and 3.

Credit Risk Management continuously updates the list of counterparties with increased credit risk and submits monthly reports to the Credit Committee meeting, which then decides on the measures to be taken.

68.5.6. Investment risk

Given the nature of the participations held, the investment risk is of minor importance. As at 31 December 2017, the book value of investments in associates (at equity) was EUR 0.0m (31/12/2016: EUR 0.0m; for details see Note 18). The book value of investments in assets available for sale amounted to EUR 2.8m (31/12/2016: EUR 3.0m).

68.5.7 Counterparty default risk from derivatives, repo transactions and securities transactions

Legally binding netting arrangements for derivatives and repo transactions (close-out netting) have been concluded with all active counterparties of Kommunalkredit. For derivatives, credit support agreements and/or collateral annexes to framework contracts providing for daily collateral margining in accordance with the bilateral collateralisation requirement of the European Market Infrastructure Regulation (EMIR) have been concluded with all active financial counterparties. The only exception are derivative agreements in the cover pool, for which framework agreements and netting arrangements have been made at market conditions (unilateral collateralisation by the counterparty, rating trigger).

The exposure to the counterparty default risk of derivatives, which is taken into account in credit risk, is defined as the residual risk from the current replacement cost (positive market value), considering CSAs and netting arrangements, plus an "add-on" for potential market value changes during the so-called "residual period of risk" between the default of the counterparty and the closing out/replacement of the derivative transaction.

Repo transactions are cleared in the form of genuine repos mainly via platforms with daily margining.

If in repo or securities lending transactions, a counterparty default risk results for Kommunalkredit from the difference between the liability/receivable and the market value of the corresponding collateral put up/received, this risk counts as exposure to the counterparty and is taken into account in credit risk.

Securities transactions are cleared exclusively on the basis of "delivery against payment" via Euroclear and/or Clearstream.

Counterparty default risk positions are limited through volume-based counterparty and credit concentration limits, on the one hand, and credit-VaR-based portfolio limits, on the other hand. Given the settlement and clearing principles described above, the counterparty default risk from derivatives, repo transactions and securities transactions is immaterial.

The counterparty default risk from derivatives is calculated as a credit valuation adjustment (CVA) according to IFRS 13. Kommunalkredit calculates CVA and DVA (debt valuation adjustment), aggregated as BCVA (bilateral CVA), on the basis of the potential exposure method by means of Monte Carlo simulations. The risk of BCVA fluctuations (BCVA risk) is determined by means of a VaR-based approach.

68.6. Liquidity risk management

Based on the ILAAP (Internal Liquidity Adequacy Assessment Process) definition, Kommunalkredit distinguishes between the structural liquidity risk, the funding risk and the market liquidity risk. The structural liquidity risk (liquidity risk in the narrow sense of the term) arises if follow-up financing for asset portfolios cannot be secured according to the maturity schedules. The funding risk is determined by the degree of diversification of funding sources and the risk of potentially restricted access to certain main funding markets under stressed market conditions. The market liquidity risk consists in a possible increase of liquidity costs due to bank-specific or idiosyncratic factors (liability-side market liquidity risk), on the one hand, and the necessary acceptance of discounts or time delays in the realisation of a position due to its relative size and/or the absence of a liquid market (asset-side market liquidity risk), on the other hand.

Kommunalkredit distinguishes between short-term (up to one year) and long-term (more than one year) liquidity management.

Central elements of liquidity risk management include the following:

- Analysis of the liquidity position
- Reporting to the Executive Board and the Supervisory Board
- Determination of the medium- and long-term funding requirements, including a liquidity plan
- Scenario-based dynamic liquidity forecast and liquidity coverage ratio (LCR) simulation
- Management and further development of the liquidity model
- Regular review and setting of internal transfer prices
- Securing of operational liquidity by defining time-to-wall hedging targets for the base case and the stress case. Thus, the survival of the bank for the defined minimum period is secured even without access to money and capital markets.
- Internal limitation of maturity transformation by setting limits on structural liquidity gaps
- Regulatory limitation of maturity transformation through the liquidity coverage ratio and the net stable funding ratio
- A liquidity emergency plan with clearly defined responsibilities, reporting requirements and measures is in place in case a liquidity crisis occurs.

Operational liquidity risk (< 1 year)

For the purposes of short-term liquidity management, the management uses short- and medium-term liquidity scenarios drawn up on a daily basis. These scenarios include not only contractually determined cash flows, but also expected cash flows from new issues, the termination of transactions, cash-out from new transactions, cash inflows from syndication agreements, retail deposits repayable on demand, repo prolongations and liquidity demand for cash collateral received (under credit support agreements/ISDA arrangements). The resulting liquidity gaps are managed daily in the short-term liquidity scenario, subsequently to be followed by monthly management.

The following table shows the expected liquidity gaps after the measures planned, the free liquidity reserve, and the net liquidity position resulting from the liquidity gap and the liquidity reserve:

31/12/2017 in EUR million	Expected liquidity gap	Available liquidity	Liquidity position
Up to one month	273.9	183.7	457.6
More than one month up to three months	97.5	16.9	114.5
More than three months up to one year	214.5	-19.8	194.7
Total	**585.9**	**180.9**	**766.8**

The comparative figures for 2016 are as follows:

31/12/2016 in EUR million	Expected liquidity gap	Available liquidity	Liquidity position
Up to one month	396.2	205.3	601.5
More than one month up to three months	-201.2	-67.3	-268.6
More than three months up to one year	237.6	-37.7	199.9
Total	**432.6**	**100.3**	**532.9**

The capital-weighted residual maturity of liabilities exceeds that of assets. Moreover, Kommunalkredit has a large portfolio of free assets eligible as collateral.

The daily management of cash collateral for derivative contracts practiced at Kommunalkredit greatly reduces the credit risk.

Structural liquidity risk (>= 1 year)

For the purposes of liquidity management and the structural analysis of its liquidity risk position, Kommunalkredit analyses the expected capital flows over the entire term of all on-balance and off-balance transactions. Overhangs from capital inflows and capital outflows are monitored by maturity range and at cumulative level and provide the basis for strategic liquidity management.

Organisation and reporting

A liquidity forecast, including an assessment of the additional liquidity available, is drawn up every other day, reported regularly to the Executive Board member in charge and submitted monthly to the full Executive Board within the framework of the RMC. In addition, weekly ALCO meetings on operational and strategic liquidity management are held. The long-term liquidity risk is monitored and managed by the monthly RMC.

Emergency plan

The bank's liquidity emergency plan specifies the tasks and the composition of emergency units to be set up in a crisis, the internal and external communication channels and, if necessary, the measures to be taken. The emergency plan permits efficient liquidity management in a market environment in crisis and is activated by clearly defined events and/or early warning indicators. In the event of an emergency, liquidity management is taken over by the emergency unit, which then decides on the specific measures to be taken.

ILAAP

Introduced alongside ICAAP within the framework of Pillar 2 of the Basel Accord, the Internal Liquidity Adequacy Assessment Process (ILAAP) serves the purpose of safeguarding the adequacy of the bank's own liquidity risk management procedures.

The individual components of ILAAP cover:

- Liquidity risk strategy and tolerance
- Organisation / policies / processes
- Risk measurement and reporting
- Stress testing
- Liquidity ICS framework
- Emergency plan
- Funding plan

All ILAAP components form an integral part of the more comprehensive ICAAP, which covers all bank-specific risks, including the liquidity risks in all its forms.

Analysis of financial liabilities

The following table shows the maturities of contractual, non-discounted cash flows of financial liabilities as at 31 December 2017 (net for derivatives, gross for cross-currency swaps, positive value for pay-out overhang):

Cash flows in EUR million as at 31/12/2017	Liabilities at amortised cost	Derivatives designated as hedging instruments	Trading*
Up to one month	147.5	1.8	3.6
More than one month up to three months	125.4	0.9	31.1
More than three months up to one year	378.7	14.1	26.6
More than one year up to five years	1,515.0	26.6	64.6
More than 5 years	1,555.3	15.7	37.1
Total	**3,721.8**	**59.1**	**163.1**

* The derivatives are not formally embedded in a micro-hedge as defined in IFRS, but serve for risk management at portfolio level. Kommunalkredit does not engage in any trading activities.

As at 31 December 2017, the nominal amount of interest-rate and currency swaps was EUR 3.1bn (31/12/2016: EUR 3,3bn).

The comparative figures for 2016 are as follows:

Cash flows in EUR million as at 31/12/2016	Liability at amortised cost	Derivatives designated as hedging instrument	Trading*
Up to one month	1855	2.0	4.6
More than one month up to three months	442.1	1.4	11.2
More than three months up to one year	228.1	14.5	18.6
More than one year up to five years	1,026.7	57.5	77.3
More than five years	1,591.5	21.3	49.3
Total	**3,473.8**	**96.7**	**161.0**

* The derivatives are not formally embedded in a micro-hedge as defined in IFRS, but serve for risk management at portfolio level. Kommunalkredit does not engage in any trading activities.

Besides redemptions, the cash flows also comprise interest payments. For liabilities with variable cash flows, future cash flows are determined on the basis of forward rates.

As a matter of principle, the amounts are allocated on the basis of their contractual rather than expected residual maturity. If the date of repayment is at the lender's discretion, the amount is allocated to the maturity range with the earliest possible redemption. Payments that have been pledged but not yet called are included in liabilities at amortised cost.

68.7. Market risk management

68.7.1. Interest rate risk

For the measurement, management and limitation of interest rate risks from positions not held in the trading book, Kommunalkredit distinguishes between the period-oriented repricing risk and the NPV-oriented risk of changing interest rates.

For the purpose of efficiently managing the interest rate risk and net interest income, Kommunalkredit uses an analysis and simulation tool (interest rate gap structure by currency, interest rate VaR, sensitivity analyses, simulation trades), which permits the forecast and targeted management of the bank's interest rate risk from positions not held in the trading book, the P&L sensitivity of the fair value portfolio according to IFRS, and net interest income for the period. To calculate the interest rate VaR, the variance/co-variance approach with a holding period of 20 trading days and a confidence interval of 95% is used, based on equally weighted historical volatilities and correlations.

Kommunalkredit's portfolio mainly comprises positions with clearly defined interest rate and capital commitment. As a rule, non-linear risks are completely hedged. Open positions are strictly limited and monitored. Retail deposits include positions without clearly defined interest rate and capital commitment (deposits repayable on demand). In principle, the interest rate commitment of deposits repayable on demand is modelled as a function of the pricing strategy. Non-linear risks that are not hedged are quantified through a scenario analysis and added to the interest rate VaR. Kommunalkredit uses the fully integrated SAP/SEM-IT system for risk quantification.

For interest rate risk management by the RCM and ALCO, the gap structures, broken down by currency, are analysed and the price sensitivity of the overall position as well as the impact of interest rate changes on the net interest income of the period (repricing risk) are quantified for different scenarios. The repricing risk is measured daily for the main currencies of Kommunalkredit (EUR, USD, CHF, JPY) and communicated to Treasury as a basis for risk management.

For risk management purposes, Kommunalkredit differentiates between the following sub-portfolios:

- less-than-twelve-months interest-rate position (short-term ALM)
- more-than-twelve-months interest-rate position (long-term ALM)
- equity investment portfolio ("equity book")
- IFRS fair value position

An analysis and management tool is used for the daily management of short-term, less-than-twelve-months interest risk positions, which permits the efficient management of the repricing risk by currency.

- Annual net interest income effect from Kommunalkredit's repricing risk as at 31 December 2017 in EUR million in the event of a parallel rise of short-term interest by +100bp:

EUR	USD	CHF	JPY	Other	Total
+4.6	0.0	-0.3	0.0	0.0	**+4.3**

- NPV risk of interest rate changes in Kommunalkredit's banking book as at 31 December 2017 in EUR million in the event of a +25bp parallel shift in the yield curve:

EUR	USD	CHF	JPY	Other	Total	VAR total
+1.7	0.0	-0.2	+1.0	-0.4	**+2.1**	**-1.1**

- NPV risk of interest rate changes of the IFRS interest-rate risk position carrying through profit or loss in EUR million as at 31 December 2017 in the event of a +25bp parallel shift in the yield curve:

EUR	USD	CHF	JPY	Other	Total	VAR total
+3.6	0.0	-0.4	-0.1	0.0	**+3.1**	**-2.1**

The comparative figures for 201 are as follows:

- Annual net interest income effect from Kommunalkredit's repricing risk as at 31 December 2016 in EUR million in the event of a parallel rise of short-term interest by +100bp:

EUR	USD	CHF	JPY	Other	Total
-1.3	0.0	-0.6	+0.1	0.0	**-1.8**

- NPV risk of interest rate changes in Kommunalkredit's banking book as at 31 December 2016 in EUR million in the event of a +25bp parallel shift in the yield curve:

EUR	USD	CHF	JPY	Other	Total	VAR total
+1.4	-0.4	-0.3	+1.6	-0.4	**+1.9**	**-5.9**

- NPV risk of interest rate changes of the IFRS interest-rate risk position carrying through profit or loss in EUR million as at 31 December 2016 in the event of a +25bp parallel shift in the yield curve:

EUR	USD	CHF	JPY	Other	Total	VAR total
+4.5	0.0	-0.6	-0.1	0.0	**+3.8**	**-3.6**

68.7.2. Currency risk

The currency risk is the risk of losses in foreign currency positions caused by an unfavourable change in the exchange rate, the open FX position being the difference between the sum total of asset positions and the sum total of liability positions, including FX derivatives, in a given currency.

To measure the risk, a VaR of the open foreign currency position according to Austrian GAAP is determined daily, based on a variance/co-variance approach with a holding period of one trading day and a confidence interval of 99%, using exponentially weighted historical volatilities and correlations.

Except for a small residual position according to Austrian GAAP, the open FX position is closed daily.

The FX VaR as at 31 December 2017 was EUR 0.011m (as at 31/12/2016: EUR 0.011m).

68.7.3. Spread widening risk

The spread widening risk is the risk of losses in value due to market-related changes in credit spreads.

The credit spread risk of P&L according to IFRS in the event of spreads widening by one basis point (CS01) amounted to EUR -0.4m as at 31 December 2017 (as at 31/12/2016: EUR -0.4m), resulting from fair value portfolios against Austrian public borrowers.

68.7.4. Basis spread risk

The basis spread risk is the risk resulting from a change in basis spread, which is factored into the variable interest rate conditions for non-standard reference interest rates and payment frequencies.

Except for residual risks, the basis spread risk is hedged in the individual currencies.

As at 31 December 2017, the basis spread risk in the event of basis spreads widening by 1 basis point was EUR +0.1m (as at 31/12/2016: EUR +0.2m).

68.7.5. Option price risk

The option price risk for Kommunalkredit is the risk of changes in the market values of open option positions.

To measure the option price risk, a scenario matrix is used to determine interest rate shifts (-/+ 50bp), volatility shifts (-/+30%) and combined shifts.

The option price risk in the banking book calculated on the basis of the scenario matrix amounted to EUR -0.8m as at 31 December 2017 (as at 31/12/2016: EUR -0.7m). However, the open option price risk in the banking book results almost exclusively from unilateral call rights of Kommunalkredit for own issues (i.e. Kommunalkredit has the right to call). As at 31 December 2017, there were no P&L-relevant option price risks.

68.8. Operational risk

Kommunalkredit defines operational risk as the possibility of losses occurring due to the inadequacy or failure of internal processes, people and systems or as a result of external events. The legal risk is part of the operational risk. External events classified as pure credit risk, market risk, liquidity risk or other types of risk with no operational background are not covered by this definition. Operational risk management (ORM) is intended to generate added value for the bank through the ORM process.

An operational risk officer and a deputy have been appointed. Operational risk correspondents (ORC), appointed by the management in consultation with the operational risk officer, act as points of contact for the individual units and support the ORM process.

An operational default database as well as risk and control self-assessments are the instruments available for the management of operational risk. The operational default database represents a retrospective view, i.e. realised gains/losses from operational events in the past are recorded in the database and cleared for further processing by the line managers in charge. Operational risk and control self-assessments represent a prospective, future-oriented view. Risks are identified and their severity is subjectively assessed. At Kommunalkredit these assessments are performed as coached self-assessments, i.e. individual risks are assessed and evaluated by the units concerned. The entries in the operational default database serve as input and provide feedback for the revaluation of risks. The management is informed about operational risks at the monthly RMS meetings and on a quarterly basis at the Executive Board meetings.

Kommunalkredit uses the standardised approach to quantify its capital adequacy requirements. The capital held on this basis is significantly in excess of actual losses suffered in the past.

68.9. Business Continuity Management

Business continuity management (BCM) ensures the adequate, comprehensive and efficient management of business continuity. This includes the elaboration and management of continuity and re-start-up plans as well as the implementation of measures designed to minimise interruptions of critical business processes. This includes the provision of alternative workplaces in the event of Kommunalkredit’s office premises being out of order.

The annual resource assessment was performed, and the resources required in the event of a crisis were established. The annual business impact analysis (BIA), performed within the framework of the resource assessment, served to assess business processes and IT services for their criticality and to verify the time to full restoration of services. The emergency plans were revised at the same time. The annual emergency exercise was performed in the fourth quarter of 2017.

69. LEGAL RISKS

No material legal risks that would have an impact on the assets, the financial position and the income of the Group were identified as of the end of the reporting period.

70. OTHER OBLIGATIONS

Liability arising from the demerger

Pursuant to § 15 (1) of the Demerger Act, Kommunalkredit is liable jointly and severally with KA Finanz AG for obligations having arisen prior to the entry of the demerger in the Companies Register on 26 September 2015 and transferred from the former Kommunalkredit to KA Finanz AG. The liability arising from the demerger is limited to the net assets allocated to Kommunalkredit at the effective date of the demerger. Obligations having arisen after the effective date of the demerger are not subject to liability arising from the demerger. Kommunalkredit does not expect to be held liable for such obligations.

Other obligations

Pursuant to § 2 (3) ESAEG, Kommunalkredit is obliged to undertake proportional safeguarding of depositors' accounts within the framework of the deposit guarantee regime of Banken und Bankiers Gesellschaft mbH, Vienna.

71. DATE OF RELEASE FOR PUBLICATION

These Consolidated Financial Statements as well as the Separate Financial Statements of Kommunalkredit were signed by the Executive Board on 5 March 2018. Both the Supervisory Board (6 March 2018) and the Annual Shareholders' Meeting (6 March 2018) can make amendments to the Separate Financial Statements, which in turn can have an impact on these Consolidated Financial Statements.

72. EMPLOYEE DISCLOSURES

From 1 January to 31 December 2017, the Kommunalkredit Group had, on average, 290 employees (1/1-31/12/2016: 272 employees), including the Executive Board; 199 of them (1/1-31/12/2106: 178) were engaged in banking operations and 91 (1/1-31/12/2016: 94) were working for KPC. 16 of the 199 employees, on average, of Kommunalkredit's banking operations were exclusively working for KA Finanz AG within the framework of a staff leasing agreement. Part-time employees are weighted according to the extent of employment.

As at 31 December 2017, the Kommunalkredit Group hat 284 employees (31/12/2016: 289 employees), including the Executive Board, 197 (31/12/2016: 195) of them engaged in banking operations and 87 (31/12/2016: 94) working for KPC.

73. RELATED PARTY DISCLOSURES

As a matter of principle, transactions with related parties are made on the same terms and conditions as transactions with independent business partners.

Ownership structure

Name of the company	Relationship with Kommunalkredit	Registered office	Shares held
Gesona Beteiligungsverwaltung GmbH	Direct parent	Vienna, Austria Comp.Reg.no 428969 m	99.78 % in Kommunalkredit
Satere Beteiligungsverwaltungs GmbH	Controlling parent	Vienna, Austria Comp.Reg.no 428981 f	100 % in Gesona

Satere Beteiligungsverwaltungs GmbH (Satere) is held by Interritus Limited (holding 55%) and Trinity Investments Designated Activity Company (holding 45%); the two shareholders exercise joint control over Satere via contractual arrangements. Thus, Satere qualifies as a joint arrangement according to IFRS 11 and therefore is to be classified as the controlling parent of Kommunalkredit.

In the current business year, Kommunalkredit took over the fiduciary management of loans for a related party of Trinity under a framework agreement. As at 31 December 2017, positions in the amount of EUR 239.2m were held in trust on the basis of a trust agreement; as Kommunalkredit has no rights or duties relative to the underlying lending business, the criteria for balance sheet recognition do not apply. Through the fiduciary management of these transactions, fee and commission income in the amount of TEUR 659.3 was generated in 2017, with open balances in the amount of TEUR 474.1 reported under “Other assets” as at 31 December 2017.

Tax group

Effective as of 2016, a tax group pursuant to § 9 of the Corporate Income Tax Act was established with Satere Beteiligungsverwaltungs GmbH as the group parent and Gesona Beteiligungsverwaltung GmbH, Kommunalkredit, KBI, KPC and TrendMind IT Dienstleistung GmbH (TrendMind) as group members (for details see Note 22).

Relations with associates

The following relations exist with Kommunalleasing, an associate included at equity:

- Loans and receivables in the amount of TEUR 37,246.4 (31/12/2016: TEUR 42,191.4)
- Contingent liabilities in the form of guarantees in the amount of TEUR 1,350.0, unchanged from the previous year
- Other off-balance-sheet obligations in the form of committed but unused lines in the amount of TEUR 1,581.0, unchanged from the previous year

Transactions with key management personnel

Key management personnel are defined as persons having direct or indirect authority and responsibility for planning, directing and controlling the activities of Kommunalkredit. At Kommunalkredit, the members of the Executive Board and the Supervisory Board qualify as key management personnel.

Executive Board and Supervisory Board remuneration

The following table shows the total remuneration earned by members of the Executive Board and the Supervisory Board:

Total remuneration in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
Active Executive Board members	1,983.3	1,299.2
Active Supervisory Board members	90.3	140.1
Total	**2,073.6**	**1,439.3**

The amounts reported under total remuneration of active Executive Board members include amounts falling due on a short-term basis. In addition, there are other long-term benefits of TEUR 478.5 (2016: TEUR 164.8) as specified in the remuneration manual (deferrals of variable remuneration) pursuant to § 39b of the Austrian Banking Act. Moreover, contributions to a pension fund were made for active Executive Board members in the amount of TEUR 217.4 (2016: TEUR 301.7).

As at 31 December 2017 and unchanged from the previous year, no loans/advances to members of the Executive Board and members of the Supervisory Board were outstanding. No guarantees were issued by Kommunalkredit for Board members.

Expenses for severance pay and pension payments mainly include changes in personnel provisions and contributions to the statutory staff pension plan as well as payments to a pension fund:

Expenses for severance pay and pensions in EUR 1,000	1/1-31/12/2017	1/1-31/12/2016
Executive Board members and senior employees	363.0	754.2
Other employees	417.4	862.2
Total	**780.4**	**1,616.4**
of which recognised in equity (change in provisions due to actuarial gains/losses)	*-992.8*	*131.6*
of which recognised in general administrative expenses	*1,773.2*	*1,484.8*

Apart from the above, there were no business relations during the reporting year and no open balances at the balance sheet date between Kommunalkredit and the members of the Executive Board and the Supervisory Board.

74. RELATIONS WITH KA FINANZ AG

Kommunalkredit Austria AG (Kommunalkredit) acts as a service provider for the banking operations of KA Finanz AG.The services to be provided are defined in a service agreement and a service level agreement. As at 31 December 2017, 15 employees (31/12/2016: 18 employees) of Kommunalkredit were working directly and exclusively for KA Finanz AG on the basis of a staff leasing agreement. They are responsible for portfolio management, risk management and the conduct of the company’s operational business under the management of the Executive Board of KA Finanz AG.

In 2017, a total of TEUR 12,105.8 (1/1-31/12/2016: TEUR 10,872.9) were invoiced to KA Finanz AG for services rendered. Receivables for services invoiced to KA Finanz AG in the amount of TEUR 3,678.8 (31/12/2016: TEUR 10,504.1) are reported under “Other assets”.

In 2018, KA Finanz AG launched a call for tenders for the services currently provided by Kommunalkredit. The bank submitted a bid for the continued provision of these services. A decision by KA Finanz AG is expected by mid-2018. If Kommunalkredit is not awarded the contract, the service agreement with KA Finanz AG will expire in the first half of 2019. In that case, Kommunalkredit will adjust its operational capacities within a contractually agreed 12-month transitional period.

Moreover, Kommunalkredit holds in trust and manages in its own name financial instruments with a nominal value of TEUR 198,856.6 (31/12/2016: TEUR 218,001.3) at KA Finanz AG's cost and risk.

75. DISCLOSURE PURSUANT TO PART 8 CRR

In accordance with the requirements of Part 8 CRR, material qualitative and quantitative information relating to the bank is published in a separate Disclosure Report, which can be accessed on the Kommunalkredit website (www.kommunalkredit.at) under "Investor Relations / Financial Information & Reports".

76. DISCLOSURES RELATING TO THE BOARDS OF THE BANK

Executive Board

Alois Steinbichler
Chairman of the Executive Board

Jörn Engelmann
Member of the Executive Board

Karl-Bernd Fislage
Member of the Executive Board
since 1 February 2017

Wolfgang Meister
Member of the Executive Board

Supervisory Board

Patrick Bettscheider
Chairman; delegated by Interritus Limited

Christopher Guth
Deputy Chairman; delegated by Attestor Capital

Friedrich Andreae
Delegated by Attestor Capital; Managing Director of Gesona Beteiligungsverwaltung GmbH and Satere Beteiligungsverwaltungs GmbH

Katharina Gehra
Delegated by Interritus Limited; Managing Director of Gesona Beteiligungsverwaltung GmbH and Satere Beteiligungsverwaltungs GmbH

Jürgen Meisch
Managing Director of Achalm Capital GmbH

Martin Rey
Managing Director of Maroban GmbH
since 24 July 2017

Werner Muhm
Former Director of the Vienna Chamber of Labour and the Federal Chamber of Labour
until 10 March 2017

Patrick Höller
Nominated by the Staff Council

Franz Hofer
Nominated by the Staff Council
until 6 November 2017

Paul Matousek
Nominated by the Staff Council
since 6 November 2017

Renate Schneider
Nominated by the Staff Council
since 20 February 2017

Vienna, 5 March 2018

The Executive Board of
Kommunalkredit Austria AG

Alois Steinbichler	**Jörn Engelmann**	**Karl-Bernd Fislage**	**Wolfgang Meister**
Chairman of the Executive Board	Member of the Executive Board	Member of the Executive Board	Member of the Executive Board

AUDIT OPINION

Report on the Consolidated Financial Statements

Audit Opinion

We have audited the consolidated financial statements of Kommunalkredit Austria AG, Vienna, and its subsidiaries (the Group), which comprise the consolidated balance sheet as at December 31, 2017, the consolidated statement of profit or loss, the consolidated statement of comprehensive income, the consolidated statement of cash flows and the consolidated statement of changes in equity for the fiscal year then ended, and the notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements comply with legal requirements and give a true and fair view of the financial position of the Group as at December 31, 2017, and of its financial performance and cash flows for the year then ended in accordance with the International Financial Reporting Standards (IFRSs) as adopted by the EU and the additional requirements under Section 59a Austrian Banking Act in conjunction with Section 245a Austrian Commercial Code.

Basis for Opinion

We conducted our audit in accordance with Regulation (EU) No. 537/2014 (hereinafter EU Regulation) and Austrian generally accepted auditing standards. Those standards require the application of the International Standards on Auditing (ISAs). Our responsibilities under those provisions and standards are further described in the "Auditor's Responsibilities for the Audit of the Consolidated Financial Statements" section of our report.

We are independent of the Group in accordance with Austrian Generally Accepted Accounting Principles and professional requirements and the requirements of the Austrian Banking Act, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

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

We have structured key audit matters as follows:

- Description
- Audit approach
- Reference to related disclosures

1. Project financing

- Description

In 2016, Kommunalkredit Austria AG, Vienna, reoriented its business model in the area of infrastructure financing. The consolidated financial statements as at December 31, 2017 include a total lending volume of EUR 2.2 billion (loans and advances to customers and credit institutions as well as contingent liabilities), of which EUR 635 million pertains to project financing newly agreed in 2017 (prior year: EUR 146 million). Whether these project financing loans – which are highly complex given their particularly individual nature – are recoverable or not depends on the expectations placed on the economic development of the financed projects as well as on the assumptions used in the measurement of the loans.

In the reporting year, Kommunalkredit Austria AG, Vienna, revised the existing loan processes particularly with regard to the project financing business and carried out adjustments to the organizational structure particularly by increasing the number of front office staff as well as by appointing a new management board member.

Given the change in the business model, the complexity of the transactions and the high degree of assumptions and expectations required in the measurement of the loans and advances, we determined the recoverability of the new transactions to be a key audit matter.

- Audit approach

With a view to evaluate the appropriateness of the processes and the measurement of the project financing, we:

- evaluated the significant lending business processes and their appropriateness,
- identified and tested the internal control system, particularly the key controls involved in approving loans, in the ongoing monitoring and the early detection process, as well as critically assessed the internal control system for the correct use of the rating models and valuation of collateral, and evaluated the appropriateness of the loan processes; we found that we can rely on the controls in place in the course of the audit,
- tested, on a sample basis, whether events occurred or will occur that significantly affect the borrower’s repayment ability with regard to loans and advances that are not considered as defaulted, in particular with a view to the assumptions made by the credit institution in the course of scenario analyses,
- evaluated the appropriateness of the risk assessment made by Kommunalkredit Austria AG, Vienna, for a sample of loans and advances. With regard to these loans and advances, we critically assessed the cash flows estimated by Kommunalkredit Austria AG, Vienna, to be received from interest, repayments and collateral so as to be able to assess the appropriateness of the risk assessment made by the credit institution stated in the consolidated financial statements,
- with a view to assess the reliability of the processes used to calculate the collective loan loss provisions, evaluated the method applied as well as the backtesting of the collective loan loss provisions by using a sample and found that the parameters used – when being considered retrospectively – were in an appropriate range,

- critically assessed, on a sample basis, the procedures in place to measure the fair values of loans and advances and reperformed the mapping of the loans and advances accounted for at their fair values in the valuation system as well as the core banking system,
- assessed the information regularly brought to management's attention at the meetings of the Risk Management Committee ("RMC") as well as in quarterly valuation meetings held at fixed dates and continuously monitored the decisions of these Committees. At the valuation meetings held at fixed dates, crucial decisions regarding the necessary credit spread adjustments in the course of changes made to models are taken.

- Reference to related disclosures

Please refer to statements made by management in items 14, 49.2, 66 and 67 in the notes to the consolidated financial statements ("notes") and in the management report for the Group.

2. Deposit business process – Online retail funding

- Description

In the fiscal year 2017, Kommunalkredit Austria AG, Vienna, implemented the online retail platform "Kommunalkredit Invest" (online retail funding). Kommunalkredit Austria AG, Vienna, offers the depositing of funds available on a daily basis or of fixed-term deposits of a period of up to 10 years to private individuals. The platform has been available to customers in Austria since September 2017 and to customers in Germany since the beginning of 2018. The volume of deposits of private customers made via the online retail platform stands at EUR 116 million as at December 31, 2017.

Kommunalkredit Austria AG, Vienna, decided to outsource material process steps regarding the acquisition and processing of transactions made via the online retail platform to FinTech Group Bank AG, Willich, Germany.

- Audit approach

We:

- evaluated the business processes implemented at Kommunalkredit Austria AG, Vienna, with regard to outsourcing online retail funding to meet the requirements under Section 25 Austrian Banking Act (BWG) and found them appropriate,
- tested the interfaces set up in the system between Kommunalkredit Austria AG, Vienna, and the service organisation,
- evaluated the presentation of the online retail funding (ORF) deposit business and the corresponding deferred interest in the balance sheet and statement of profit and loss of Kommunalkredit Austria AG, Vienna,
- assessed the agreements with the service organisation (Service Level Agreement dated May 12, 2017, service tickets, operating procedures, etc.),
- satisfied ourselves of the effectiveness of the implemented processes and controls in the course of an on-site visit to the service organisation,
- critically assessed the process and the controls for the automated interest calculation and establishing the customers' quarterly information (account notifications) and reperformed the calculation,
- inspected the internal audit reports as well as the audit reports of the Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*, BaFin) on "money laundering and compliance" of the service organisation and with regard to serious deficiencies.

- Reference to related disclosures

Please refer to statements made by management in items 38, 50 and 54 in the notes to the consolidated financial statements (“notes”) and in the management report for the Group.

3. Hedge accounting with regard to derivatives

- Description

Kommunalkredit Austria AG, Vienna, uses a large number of interest and cross currency swaps to hedge its interest rate and currency risk. Hedging is made at single item level using fair value hedges. Kommunalkredit Austria AG, Vienna, uses interest rate swaps and interest rate cross currency swaps as hedging instruments that are accounted for at their fair values. Gains and losses from measurement changes are shown in the “trading and valuation result”.

The volume of the derivatives used to hedge the interest rate and currency risks shows a nominal amount of EUR 2.2 billion and EUR 27 million, respectively, with a positive market value on the assets side of EUR 221 million and EUR 1 million (positive market values of the interest and currency derivatives, respectively) and a negative market value on the liabilities side of EUR 74 million and EUR 3 million (negative market values of the interest and currency derivatives, respectively) with a negative valuation result from fair value hedges in the amount of EUR 1 million.

The high volume of interest and cross currency swaps represents a key audit matter with regard to the question whether all hedges meet the requirements of IAS 39 and are presented in the consolidated financial statements in accordance with IFRSs.

- Audit approach

We

- evaluated and critically assessed the business process in place for entering into new derivatives,
- tested key controls with regard to hedges and confirmed their appropriateness,
- determined how the prospective effectiveness measurement was performed on a sample basis,
- determined, on a sample basis, how the retrospective effectiveness measurement was performed,
- critically assessed, for dissolved hedges, the reasons stated for their dissolution and if the purposes of the hedges remain,
- evaluated the presentation of the hedges in the consolidated financial statements in accordance with the provisions laid down in IAS 39 and assessed their appropriateness,
- checked if appropriate valuation methods have been selected and consistently applied, and
- evaluated the process used to measure individual transactions by taking into account the hedging relationship,
- examined and reconciled the risk management guidelines in place for entering hedges, as well as
- reperformed the recognition of effects on the result due to fair value hedges.

- Reference to related disclosures

Please refer to statements made by management in items 15, 30 and 49 in the notes to the consolidated financial statements (“notes”).

Responsibilities of Management and the Audit Committee for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU, and the additional requirements under Section 59a BWG and Section 245a UGB, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

The audit committee is responsible for overseeing the Group’s financial reporting process.

Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the EU Regulation and with Austrian generally accepted auditing standards, which require the application of 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 consolidated financial statements.

As part of an audit in accordance with the EU Regulation and with Austrian generally accepted auditing standards, which require the application of ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risks of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control,
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group’s internal control,
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management,
- conclude on the appropriateness of management’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are

based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern,

- evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation,
- obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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

Report on Other Legal and Regulatory Requirements

Comments on the Management Report for the Group

Pursuant to the Austrian Commercial Code, the management report for the Group is to be audited as to whether it is consistent with the consolidated financial statements and as to whether the management report for the Group was prepared in accordance with the applicable legal requirements.

Management is responsible for the preparation of the management report for the Group in accordance with the Austrian Commercial Code and the Austrian banking provisions.

We conducted our audit in accordance with Austrian Standards on Auditing for the audit of the management report for the Group.

Opinion
In our opinion, the management report for the Group was prepared in accordance with the applicable legal requirements and is consistent with the consolidated financial statement.

Statement
Based on the findings during the audit of the consolidated financial statements and due to the obtained understanding concerning the Group and its circumstances no material misstatements in the management report for the Group came to our attention.

Other information

Management is responsible for the other information. The other information comprises the information included in the annual report, but does not include the consolidated financial statements, the management report for the Group and the auditor’s report.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated 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 of this other information, we are required to report that fact. We have nothing to report in this regard.

Additional Information in Accordance with Article 10 of the EU Regulation

We were appointed as statutory auditor at the ordinary general meeting dated April 7, 2016. We were engaged by the supervisory board on April 7, 2016. We have audited the Company for an uninterrupted period since its foundation in 2015 (three years). In that year, the operating business of Kommunalkredit Austria AG, Vienna, Austrian Companies Register no. 439528s, was spun off to Kommunalkredit Austria AG, Vienna, Austrian Companies Register no. 45776v (“KA old”). We had audited KA old since 2010.

We confirm that the audit opinion in the “Report on the Consolidated Financial Statements” section is consistent with the additional report to the audit committee referred to in Article 11 of the EU Regulation.

We declare that we did not provide any prohibited non-audit services (Article 5 (1) of the EU Regulation) and that we remained independent of the audited company in conducting the audit.

Responsible Engagement Partner

Responsible for the proper performance of the engagement is Ms. Dorortea-E. Rebmann, Austrian Certified Public Accountant.

Vienna, March 6, 2018

PwC Wirtschaftsprüfung GmbH

signed:

Dorotea-E. Rebmann

Austrian Certified Public Accountant

This report is a translation of the original report in German, which is solely valid. Publication and sharing with third parties of the consolidated financial statements together with our auditor’s opinion is only allowed if the consolidated financial statements and the management report for the Group are identical with the German audited version. This audit opinion is only applicable to the German and complete consolidated financial statements with the management report for the Group. For deviating versions, the provisions of Section 281 (2) UGB apply.

STATEMENT BY THE LEGAL REPRESENTATIVES

Kommunalkredit Group

Consolidated Financial Statements 2017

We herewith confirm to the best of our knowledge that the **Consolidated Financial Statements** prepared in accordance with the relevant accounting standards, present a true and fair view of the assets, the financial position and the income of the Group, that the Management Report presents the development of business, the results and the position of the Group in such a way that it conveys a true and fair view of the assets, the financial position and the income of the Group, and that the Management Report describes the essential risks and uncertainties to which the Group is exposed.

Vienna, 5 March 2018

The Executive Board of
Kommunalkredit Austria AG

Alois Steinbichler	**Jörn Engelmann**	**Karl-Bernd Fislage**	**Wolfgang Meister**
Chief Executive Officer	Member of the Executive Board	Member of the Executive Board	Member of the Executive Board

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