# *Annual Report 2014*

*“Money must serve, not rule.”*

*His Holiness Pope Francis, Evangelii Gaudium, 2013*

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CHAPTER 1

# Introduction by the Commission of Cardinals

The Commission of Cardinals welcomes the publication of the 2014 Annual Report of the Istituto per le Opere di Religione, which is made public in accordance with the Institute's regulatory obligations under Vatican law.

Last April, the Holy Father reaffirmed the importance of the Institute's continuing role in assisting the Holy See in carrying out the Holy Father's work as universal pastor and in aid of those institutions and individuals who work with the Holy Father.

With the publication of our annual report, we warmly welcome Cardinal Josip Bozanic as the sixth member of the Commission of Cardinals, as well as our new Board of Superintendence, comprising: President Jean-Baptiste Douville de Franssu, Clemens Boersig, Mary Ann Glendon, Sir Michael Hintze, Mauricio Larraín, Carlo Salvatori, and Msgr. Alfred Xuereb (who joins the Board as non-voting Secretary). As we extend our welcome to the new Board members, we would like to express our gratitude for the years of service provided by our previous Board members, who worked hard and accomplished much.

Finally, we would like to extend our warm appreciation to the Institute's permanent personnel and renew our gratitude for their dedication and hard work. It is our employees – those men and women who have made their careers here at the Institute – who understand well that serving the "universal mission" is not a label for the Institute, but a commitment to helping people.

Santos Card. Abril

*Cardinal Santos Abril y Castelló*
*President of the Commission of Cardinals*
*Istituto per le Opere di Religione*

CHAPTER 2

# Introduction by the Prelate

As I noted in my message last year, it is of vital importance to remember the IOR's purpose. That purpose is not to pursue the accumulation of wealth. Rather, it is to honestly and faithfully serve the universal mission of the Church by supporting those who work in the vineyards of the Lord – often thanklessly and under dangerous circumstances – to feed, to educate, to heal, and to permit the gospel to be known.

This is the service that I hope and pray shall remain the focus of the IOR as the future unfolds.

> La mia preghiera è che l'Istituto lavori non semplicemente per far crescere un patrimonio perché questo, in sé, è totalmente privo di significato. Invece, mi auguro che l'Istituto vada verso una trasformazione per "consentire ai principi del Vangelo di permeare anche le attività di natura economica e finanziaria".

Finally, I would like to take this opportunity to thank those members of the staff of the IOR who have demonstrated their dedication, kindness and professionalism.

*Msgr. Battista Mario Salvatore Ricca*
*Prelate*
*Istituto per le Opere di Religione*

CHAPTER 3

# Introduction by the President

Dear Readers,

2014 was in many ways another year of profound change at the IOR.

First, a new board was nominated on 9 July, which I have the honour of chairing. It is composed of senior business and academic leaders from Europe, USA, South America, and Australia, who bring with them considerable expertise in financial matters. Their time and contribution is critical to the future of the IOR.

Second, the work that was started by the previous board and its chairman Ernst von Freyberg – notably in the field of anti-money laundering (AML) and Know Your Customer (KYC) with the adoption of Vatican rules and regulations – was either deepened further in 2014, or completed. I would like to express my sincere appreciation for the tireless efforts of the previous board.

Third, significant progress has been achieved in the last twelve months in adapting the IOR to the new Holy See regulatory environment, reviewing the IOR's interaction with tax authorities around the world, and addressing the misuse the IOR was subjected to in the past.

At this point, I should note the level of the Institute's operating profit for 2014, which was essentially the result of financial market developments during these 12 months, in the light of the composition of the IOR's proprietary portfolio.

In parallel to all these essential efforts, we have done a lot of work to define a new way forward for the Institute to fulfil its mission to support the Holy Father in his work to help the poor, and in the propagation of faith. That has taken up much of the time and focus of the IOR's management team over the last few months, and as I write this introduction the team is finalising with the board the last component of a long-term plan for the IOR's future.

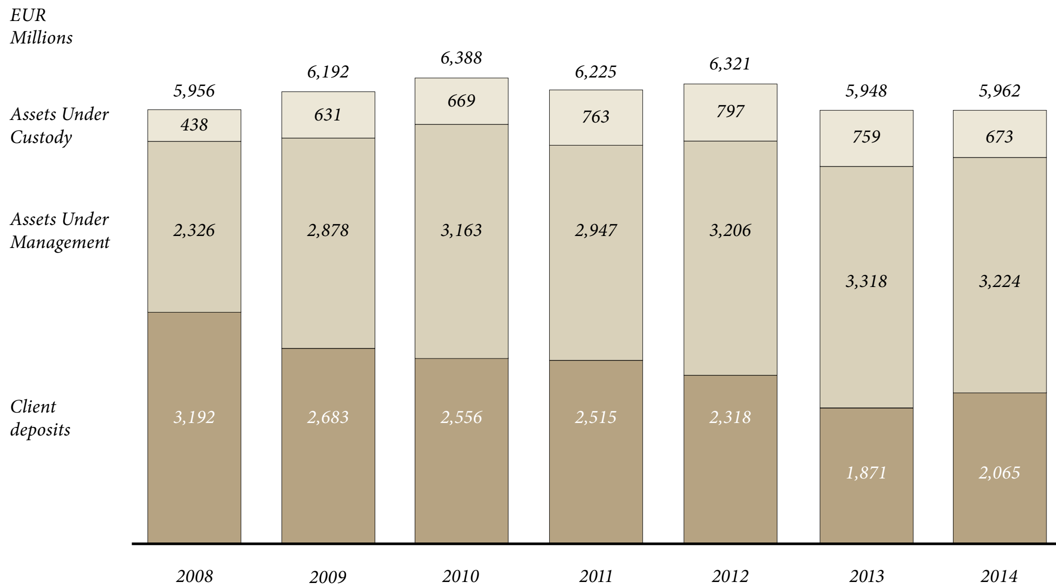
This plan revolves around two key objectives. First, putting the interests of the clients first by offering appropriate products, and increasing the quality of the service overall. Second, de-risking the services offered by the Institute through the development of a strategy that will allow the IOR to sustain and grow its annual contribution to the Holy See.

Clearly the first objective is the predominant one. Without satisfied clients, the client base of the IOR will reduce and the IOR will no longer be able to contribute to the Holy See's finances.

All the contacts that I have had with the IOR's clients (congregations, dioceses) confirm the need for the Institute to develop asset management solutions and move away from term deposits. Our clients are in fact already anticipating this shift, as the evolution of our clients' assets demonstrate.

In fact, from 2008 to 2014, Client Deposits decreased from EUR 3.2bn to EUR 2.1bn while Assets Under Management increased from EUR 2.3bn to EUR 3.2bn.

Evolution of client assets:




To proceed in this direction, the main challenge of the Institute is thus to fundamentally improve the performance of our asset management services, and ensure that we improve our client service standards. This is what is at the core of the new strategic plan. By doing so we will de-risk, stabilise and ultimately grow a stream of recurring revenue for the IOR and the Holy See. In parallel, all efforts will be undertaken to provide seamless and reliable payment solutions.

As soon as the final decisions are made on the IOR's strategic plan, we will advise our clients, and diligently work towards delivering on those objectives. I know that the employees of the IOR are excited about these changes and we have created many opportunities to meet internally in large and small groups in order to keep everyone informed of the progress made.

I would like to take this opportunity to thank the whole team at the IOR.

We have many talented individuals who have over the year shown dedication and loyalty to the Institute and the Church. It is a privilege for me to work with them.

Finally, let me also express my gratitude to our customers. We exist because of them and they should be assured that we are working hard to keep improving the quality of the service we provide to them.

*Jean-Baptiste Douville de Franssu*
*President of the Board of Superintendence*
*Istituto per le Opere di Religione*

CHAPTER 4

# A Business Review of 2014



## a) Macroeconomic environment

The following gives an overview of the macroeconomic environment in 2014, with a particular focus on those markets and developments most relevant to explaining the IOR's portfolio performance, given its conservative investment strategy.

Low inflation across developed economies became of particular concern in the Eurozone, raising fears that it might slide into Japan-style stagnation. In response, the European Central Bank (ECB) cut interest rates twice, initiated a programme of cheap four-year lending (TLTROs) and launched programmes to purchase covered bonds and asset-backed securities.

The divergence in monetary policy was clear: the Fed and Bank of England were expected to start raising interest rates over the next 12 months while the ECB and Bank of Japan (BoJ) remained firmly in easing territory. Emerging markets started to stabilise after their earlier volatility – but there was unease over the shadow banking sector in China. The world's second-largest economy also showed signs of struggling to meet its government's 7.5 % GDP growth target for the year.

Concerns persisted over the outlook for global growth as geopolitical risks heightened during the summer, in Ukraine and throughout the Middle East. This provided an ideal environment for bond yields to rally lower. By August, the ten-year German bund yield had broken below 1 % for the first time, and other European bond yields plumbed historic lows. This culminated in widespread volatility in mid-October as global equity markets plummeted and investors fled to the safety of government bonds, sending yields sharply lower. The VIX "fear gauge" spiked to its highest level since the depths of the Eurozone crisis in 2012.

Another major trend in the year was the weakness in oil prices, which gathered momentum from October as oversupply became apparent. Brent crude ended the year at USD 57 a barrel – down more than 50 % from June – after OPEC decided in November not to curb supply. Cheaper oil has heightened disinflationary pressures – and data in early 2015 showed signs that the Eurozone slipped into deflation in December. With the year ending in such fashion, sovereign QE in Europe started looking a fair bet, as ECB discussions moved beyond legal objections to focus instead on practical issues around implementation.

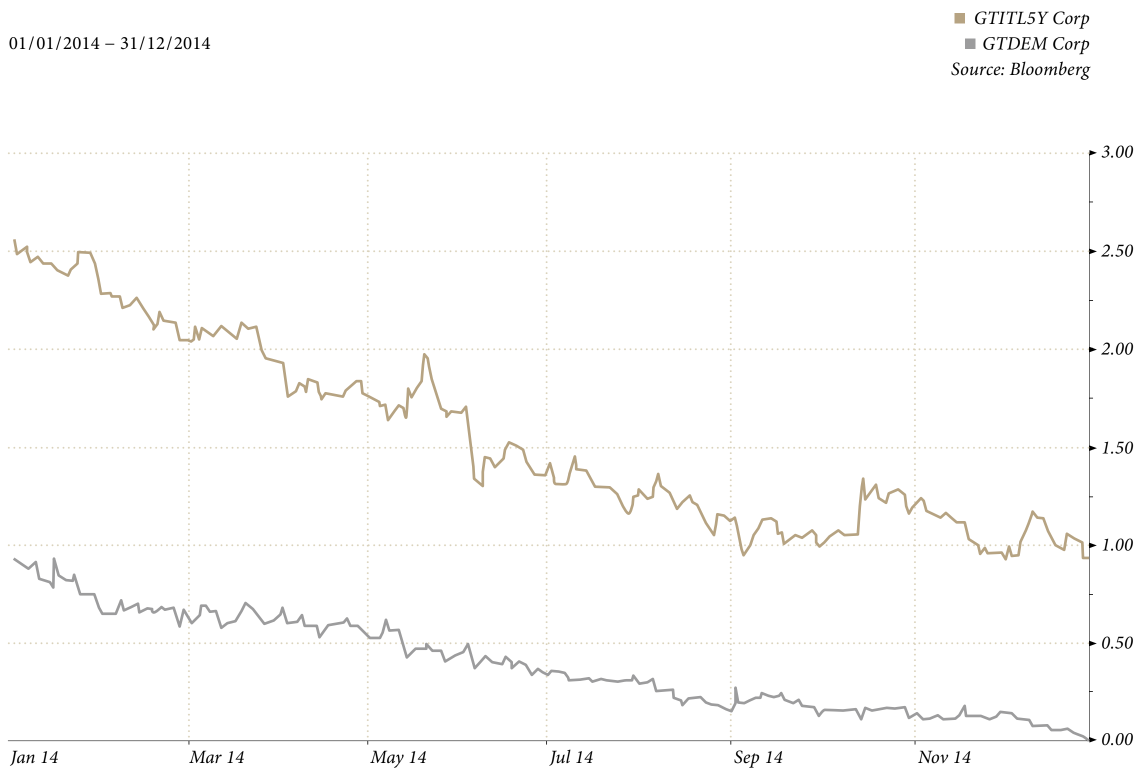
European investment-grade (IG) credit outperformed US and UK counterparts amid mounting expectations of further ECB easing. Falling oil prices negatively impacted the US corporate bond market, which has a high exposure to energy. The market was further dampened by considerable supply, with November's USD 120 bn the second-highest month ever in issuance of US IG bonds, and issuance over 2014 of USD 1.1 tn. IG outperformed high yield, with the latter experiencing severe volatility in July / August, October and December.

2014 saw significant compression in European sovereign yields, both core and peripheral, due to the expectation of central bank actions. Investment grade corporate bond spreads tightened across the ratings spectrum. High yield bond spreads also compressed, but with more volatility than IG.

European GDP growth remained relatively stagnant, but showed signs of a potential rebound in YE 2014. Household consumption drove much of the positive growth – but was weighed down by investment and inventory levels.

Inflation in the Eurozone remained low throughout the year and turned negative by early 2015. The ECB will be actively watching the continued deflationary pressures as quantitative easing commences. Unemployment rates saw some divergence between Germany, UK and the peripherals. Spanish unemployment continued to decline, but remains above 20 %.

Five-year Italian government bonds:
Five-year German Bunds:



Gold Price:

EUR / USD:

## b) Evolution of customer base

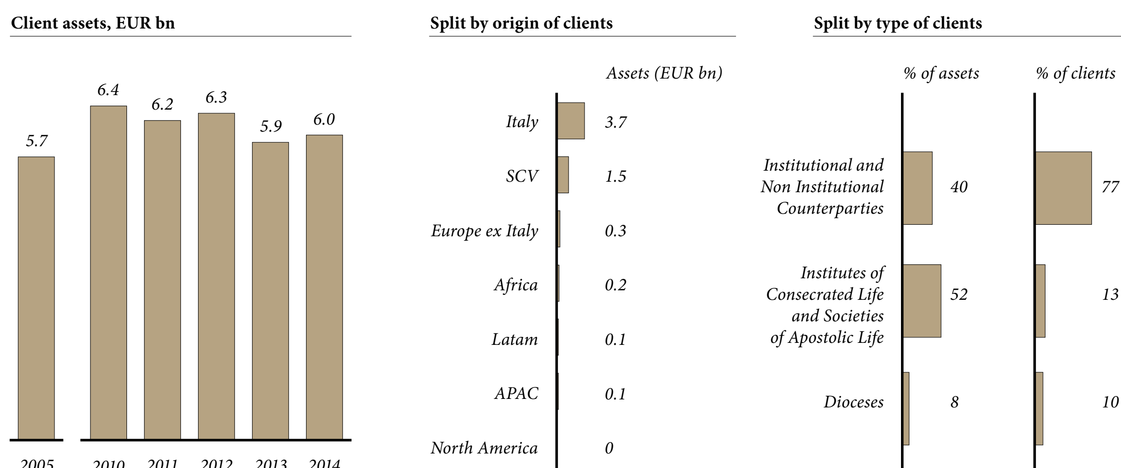
As of the end of 2014, the IOR had 15,181 customers (2013: 17,419), of which the vast majority, measured by assets entrusted to the Institute, were institutional. The IOR's customers all have one thing in common: they are part of the Catholic Church and serve it.

In 2013, the IOR updated its guidelines on the customers served by the Institute. These are the Institutional counterparties (Sovereign Institutions of the Holy See and Vatican City State and related entities, embassies and diplomats accredited to the Holy See), Non Institutional counterparties (employees and pensioners of the Vatican), Institutes of Consecrated Life and Societies of Apostolic Life and Dioceses.

As well as depositing funds with us, our customers also ask us to manage portfolios of assets on their behalf or act as custodians. As of 31 December 2014, the net value of assets held in managed portfolios was EUR 3.2 bn (2013: EUR 3.3 bn), the net value of assets held in non-managed portfolios was EUR 673.2 m (2013: EUR 758.8 m) and the value of customer deposits was EUR 2.1 bn (2013: EUR 1.9 bn), resulting in EUR 6 bn in total client assets (2013: EUR 5.9 bn).

The most important group by assets was religious orders. These accounted for half of our customers in 2014, followed by Holy See Offices and nunciatures (14 %), cardinals, bishops and clergy (9 %), dioceses (8 %), with the remainder split between various others, such as Vatican employees and institutes of religious education.

Overview of IOR clients:




The IOR engaged in a systematic screening of all existing customer records in order to identify missing or insufficient information required for the completion of new customer identity data templates, which the Institute introduced in May 2013. That task has been concluded.

AML and KYC reviews are part of the day-to-day activities, and the IOR continues to invest in strengthening its tools and processes.

In 2013, the Board of Superintendence decided to restrict the customer categories of the Institute to Catholic institutions, clerics, employees or former employees of the Vatican with salary and pension accounts, as well as embassies and diplomats accredited to the Holy See.

As of 31 December 2014, the IOR had a total of 15,181 clients. Since May 2013, the IOR has recorded the closure of 4,614 customer relationships, and the opening of 1,066 new relationships.
As of 31 December 2014, 274 remain to be closed, of which 148 will be closed by the end of May 2015.

| *Overview client relationships* | *As of 31 December 2014* |
|---|---|
| *Client relationships – Existing* | *15,181* |
| *Client relationships ended since May 2013* | *4,614* |
| *of which: Actively terminated – dormant (low balance, inactivity)* | *2,600* |
| *of which: Actively terminated – did not fit client category* | *554* |
| *of which: Closed due to natural attrition* | *1,460* |
| *New client relationships since May 2013* | *1,066* |

| *Relationships in process of being closed* | *As of 31 December 2014* |
|---|---|
| *Client relationships to be closed – Total* | *274* |
| *of which: blocked* | *126* |
| *of which: open* | *148* |

## c) Income Statement and Net Profit for the Year

In 2014, the IOR's Net Profit was EUR 69.3 m (2013: EUR 2.9 m). This increase from 2013 was mainly due to an increase in the Net Trading Income from securities and to a decline in extraordinary operating expenses.

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

The **Net Interest Result** declined 5.8 % to EUR 50.7 m in 2014, from EUR 53.8 m in 2013.

This result was mainly affected by the decline in average invested amounts to EUR 3.1 bn (2013: EUR 3.6 bn). In 2014, the IOR recorded a decrease in the yield on investments in securities and bank deposits and a decline in interest paid to clients.

The average rate on client deposits declined to 0.4 % in 2014 from 0.71 % in 2013, while the average yield on investments in securities and bank deposits declined to 1.94 % from 2.11 % in 2013. Consequently, the spread between the average rate received on assets and the average rate paid on liabilities rose to 1.54 % from 1.40 %. The Institute achieved its interest margin by consolidating short-term funds and investing for longer periods at higher rates, while ensuring sufficient liquidity to meet any obligations that might fall due.

**Net Fee and Commission Result** rose 2.1 % to EUR 14.4 m in 2014 from EUR 14.1 m in 2013. Fee and Commission Income fell 5.1 % to EUR 16.7 m in 2014, from EUR 17.6 m in 2013.

At the same time, Fee and Commission Expense fell to EUR 2.3 m in 2014 from EUR 3.5 m in 2013 (– 34.3 %).

The most important part of the Fee and Commission Income was commissions from Asset Management services, which fell 5.3 % to EUR 12.6 m in 2014 from EUR 13.3 m in 2013. This was due to the slight decline in customer assets managed by the Institute in 2014.

The decline of Fee and Commission Expense was mainly due to the decline in commission paid for securities transactions, to EUR 0.6 m in 2014 from EUR 1.6 m in 2013 (– 62.2 %) and the reduction in fees paid to banks, which was EUR 662,000 in 2014, down from EUR 836,000 in 2013 (– 20.8 %). This was a consequence of fewer transactions related to equity portfolio management, as well as the rationalisation of the IOR's external banking relationships.

The **Net Trading Result** recorded a net gain of EUR 36.7 m compared to a net loss of EUR 16.5 m in 2013.

The significant increase in the Net trading result was due mainly to the positive performance of bond markets in 2014, compared to 2013, as a result of lower interest rates. Furthermore, in 2013 the IOR recorded significant unrealised losses on external investment funds, which were not repeated in 2014.

The increase of this item is mainly due to the unrealised result from debt securities and bonds (in 2014, a gain of EUR 10.7 m, compared to a loss of EUR 6 m in 2013); the increase in realised result from debt securities and bonds (in 2014, a gain of EUR 14.8 m, compared to a gain of EUR 5.3 m in 2013); less impairment on external investment funds (in 2014, a loss of EUR 2.5 m, compared to a loss of EUR 18.3 m in 2013); the growth of realised result from external investment funds (in 2014, a profit of EUR 10.3 m, up from EUR 0.4 m in 2013) and the increase in the value of gold, which led to a gain of EUR 0.6 m as opposed to a loss of EUR 11.5 m in 2013.

**Dividend Income** fell 26.3 % to EUR 2.8 m from EUR 3.8 m in 2013.

**Operating Expenses** were EUR 28.9 m in 2014 (2013: EUR 32.2 m). This includes staff expenses of EUR 10.8 m in 2014 (2013: EUR 12 m, or – 10 %).

On 31 December 2014, the IOR had a total of 112 personnel (2013: 115). During the year, the IOR hired three new employees, three employees resigned, and three retired.

**Other Operating Expenses** fell 10.3 % to EUR 17.5 m (2013: EUR 19.5 m). This was due to the termination of some projects, including some related to meeting international anti-money laundering and compliance requirements.

**Impairment losses** were EUR 7.2 m (2013: EUR 5.7 m) mainly due to unrealised losses on investment equities available for sale (EUR 2 m) and on loans and advances to customers (EUR 2.2 m).
The item also saw a further impairment related to a zero-interest loan granted in 2013 in accordance with the mission of the Institute (EUR 1.6 m), and an impairment related to guarantees and commitments towards third parties (EUR 1.4 m).

The item **Other Net Income (Expense)** posted a positive result of EUR 0.9 m (2013: loss of EUR 14.4 m) due to the partial repayment of loans that were totally or partially written down during the previous years.

The **Net Profit** for the year of EUR 69.3 m will permit a provision of EUR 14.3 m to the Retained earnings reserve, allowing the IOR to transfer EUR 55 m to the Holy See.

## d) Balance Sheet

As of 31 December 2014, the IOR's balance sheet total was EUR 3.2 bn (2013: EUR 3.4 bn), with equity of EUR 695 m (2013: EUR 720 m).

On the Liabilities side, **Due to depositors** was the most significant item, representing 93.9 % of total liabilities on the balance sheet. This item, amounting to EUR 2.4 bn from EUR 2.5 bn in 2013, recorded a decline of EUR 182.4 m (– 7.2 %). Customer deposits grew by EUR 194.1 m, while asset management liquidity decreased EUR 376.5 m due to the department's decision to invest more in securities following the reduction of yields.

Our customers require us to invest the funds entrusted to us in a prudent manner, and to ensure that these funds are readily available for their needs. As a result, we invest predominantly in highly liquid, interest-bearing securities and with banks. Our investment in the equity markets or similar financial instruments is small. The same is true for any loans we have made. We do not borrow in the interbanking market and we do not issue debt securities.

Consequently, the asset side of the balance sheet mainly consists of bank deposits and securities.

**Bank Deposits** totalled EUR 551 m at the end of 2014 (2013: EUR 677.2 m). These mainly consisted of EUR 283.3 m in deposits on demand (2013: EUR 274.6 m), and EUR 266 m in term deposits and money market investments (2013: EUR 379.6 m). At the closing date of the financial statements, the maximum maturity of term deposits did not exceed nine months, except for a term deposit with APSA, which had a maturity longer than one year.

The IOR held **Securities** (bonds, equities and external investment funds) worth EUR 2.6 bn in 2014 (2013: EUR 2.6 bn).

Bonds, at EUR 2.5 bn, were the most significant investments, representing 96 % of the securities held as of 31 December 2014, while equities accounted for 1 %, and external investment funds for 3 %.

As already explained, the volumes of the invested amounts was little changed, but there was some change in the mix of portfolio securities: a decrease in equities and externally managed investment funds, and more investments in bond securities, in line with the aim of de-risking the portfolio.

The key features of the assets in our balance sheet as of 31 December 2014 were as follows:

| ASSET CLASSES | | |
|---|---|---|
| | *Amount 31 December 2014* | |
| | *EUR 000* | % |
| **CASH AND BANK DEPOSITS** | | |
| Cash | 16,351 | |
| Bank deposits | 551,007 | |
| | 567,358 | 17.67 |
| **TRADING SECURITIES** | | |
| Debt securities | 1,627,870 | |
| Equity securities | 13,005 | |
| External investment funds | 77,261 | |
| | 1,718,136 | 53.51 |
| **LOANS AND RECEIVABLES SECURITIES** | | |
| Debt securities | 187,677 | 5.85 |
| **AVAILABLE FOR SALE SECURITIES** | | |
| Equity securities | 10,390 | 0.32 |
| **HELD TO MATURITY SECURITIES** | | |
| Debt securities | 645,054 | 20.09 |
| Other assets | 82,160 | 2.56 |
| **Total Assets** | **3,210,775** | **100.00** |

CHAPTER 5

# Mission, Services, Customers and Charity Funds



*The IOR will continue to serve with prudence and provide specialised financial services to the Catholic Church worldwide. The valuable services that can be offered by the Institute assist the Holy Father in his mission as universal pastor and also aid those institutions and individuals who collaborate with him in his ministry.*

## a) Mission of the Institute

The Istituto per le Opere di Religione (the Institute or IOR) is an institute of the Holy See, founded on 27 June 1942 by Papal Decree, with the task of serving the Holy See and the Catholic Church all over the world. Its origins date back to the "Commissione ad Pias Causas" established in 1887 by Pope Leo XIII.

The IOR's purpose is set out in its Statute, revised by Pope John Paul II in 1990. It is "to provide for the custody and administration of goods transferred or entrusted to the Institute by physical or juridical persons, designated for religious works or charity. The Institute can accept deposits of assets from entities or persons of the Holy See and of the Vatican City State".

The IOR strives to serve the global mission of the Catholic Church by protecting and growing the patrimony of and providing payment services to the Holy See and related entities, religious orders, other Catholic institutions, clergy, employees of the Holy See and the accredited diplomatic corps.

In 2013, the IOR updated its guidelines on the customers served by the Institute. These are Institutional counterparties (Sovereign Institutions of the Holy See and Vatican City State and related entities, embassies and diplomats accredited to the Holy See), Non Institutional counterparties (employees and pensioners of the Vatican), Institutes of Consecrated Life and Societies of Apostolic Life and Dioceses.

The IOR is situated exclusively on the sovereign territory of the Vatican City State. It is subject to the regulations and legislation applicable in the Vatican City State. The IOR is supervised and regulated by the "Autorità di Informazione Finanziaria" (AIF), the financial regulatory body for the Vatican City State and the Holy See.

## b) Nature of the Institute's services

The IOR serves the global mission of the Catholic Church by safeguarding assets. It offers deposit taking, asset management, custodial functions and international payment transfers through correspondent banks, and holds salary and pension accounts of employees of the Holy See and the Vatican City State.

It protects its customers' deposits and assets by investing predominantly in government and corporate bonds and money market accounts. Less than 5 % of total assets are held in externally managed investment funds and equities.

All financing activity was carried out on a residual basis, and strictly in accordance with the mission of the Institute.

The IOR does not issue, underwrite or place securities.

According to the requirements of Vatican City State Law, customer accounts at the IOR are held in the name of the respective customer. There are no anonymous accounts. Customers are provided with services in the IOR offices in the Vatican City State. The IOR has no other locations and does not offer internet-based services.

## c) Definition of IOR customers

In many cases, our customers are active in the mission or perform charitable works at institutions such as schools, hospitals or refugee camps. Other customers are Institutional counterparties (Sovereign Institutions of the Holy See and of Vatican City State and related entities, embassies and diplomats accredited to the Holy See), Non Institutional counterparties (employees and pensioners of the Vatican), Institutes of Consecrated Life and Societies of Apostolic Life and Dioceses.

The IOR does not accept individuals without a relationship to the Holy See as customers, nor does it accept business customers.

It is in the nature of the Catholic Church that its institutions, missionary activities and charitable works reach out into parts of the world that are remote, and have very basic infrastructure, often with an underdeveloped banking and payments system. For these customers, the IOR is particularly important as a trusted, reliable and effective institution, keeping funds safe for future use or sending funds to the countries in which they operate.

Our customers are frequently located in different countries and use different local currencies. Here, too, the IOR can help safely transfer funds from one part of the world to another.

Our customers tell us that this trusted relationship is very valuable to them, especially in times of political upheaval and financial instability. Our customers also know that their money is invested responsibly and ethically.

*A typical customer would be a congregation operating in a developing country to educate children, provide health care or serve in a missionary capacity. To carry out this work, they rely on funding from other parts of the world – money that goes towards building churches, new schools, digging wells, or paying the salaries of local employees, for example.*

*The IOR serves the congregation by transferring these funds in a secure and cost-effective way, taking care of any necessary currency transactions, and guaranteeing compliance with anti-money laundering rules, embargo lists, and the like. Since the IOR does not have branches abroad, it relies on trusted correspondent banks around the world to transfer the funds on the customer's behalf.*

*The congregation will thus hold an account at the IOR in the Vatican City State where funds are collected for transfer, kept secure and conservatively managed until the funds are required. In many cases, our customers have held their account for many decades, and enjoy a relationship with the IOR based on many years of trust and experience.*

## d) Charity Funds

Alongside its day-to-day work, the IOR also maintains five charitable funds, financed through contributions from donations, including bequests and the IOR's profits, which have made significant charitable disbursements over the years. These include a fund for missionary activities, a fund for Holy Masses, a fund at the disposal of the Board of Superintendence, a deposit at the Commission of Cardinals' disposal as well as a fund at the disposal of the same Commission.

CHAPTER 6
# Corporate Governance



The IOR's governance structure is defined in the IOR's Statutes of 1990. It consists of five elements: Commission of Cardinals, Prelate, Board of Superintendence, Board of Statutory Auditors and Directorate.

*Group photo of Commission of Cardinals, Prelate and Board of Superintendence*

The number of Cardinals and board members was increased on 10 January 2015 by way of a Rescriptum ex audientia Ss.mi, elevating the number of members in the IOR Commission of Cardinals and the IOR Board of Superintendence from five to six respectively. In addition, the nomination of a non-voting Secretary General to the IOR Board of Superintendence was formalised by the President of the Commission of Cardinals.

The **Commission of Cardinals** currently consists of the following six Cardinals:

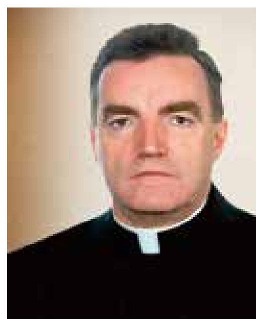
**Cardinal Santos Abril y Castelló**
*President*
*Archpriest of the Papal Basilica of St Mary Major*

**Cardinal Thomas Christopher Collins**
*Archbishop of Toronto*

**Cardinal Pietro Parolin**
*Secretary of State*

**Cardinal Christoph Schönborn**
*Archbishop of Vienna*

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



**Cardinal Josip Bozanic**
*Archbishop of Zagreb*

The Commission of Cardinals meets on a regular basis to review financial statements. The members of the Commission are appointed for a five year term, which can be renewed. It also oversees adherence to statutory norms and appoints the members of the Board of Superintendence.

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

**Msgr. Battista Mario Salvatore Ricca**
*Appointed ad interim*

The Prelate acts as secretary of the meetings of the Commission of Cardinals and attends the meetings of the Board of Superintendence.

The **Board of Superintendence** is nominated by the Commission of Cardinals and currently consists of six members and a non-voting secretary. The Board of Superintendence defines strategy and ensures oversight of operations. Each board member serves for a five-year term, which can be renewed.

**Jean-Baptiste Douville de Franssu**
*President*

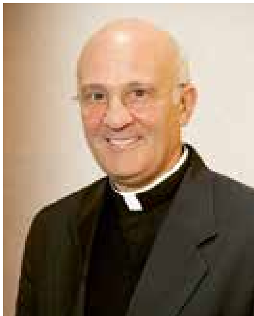
**Dr. Clemens Boersig**

**Prof. Mary Ann Glendon**

**Sir Michael Hintze**

**Mauricio Larraín**

**Carlo Salvatori**



**Msgr. Alfred Xuereb**
*Non-voting Secretary*

Until July 2014, the Board consisted of the following:

- Ernst von Freyberg, President
- Dr. Hermann Schmitz, Vice-President
- Carl A. Anderson, Non-executive member
- Antonio Maria Marocco, Non-executive member
- Manuel Soto Serrano, Non-executive member

The **Board of Statutory Auditors** consists of three members, appointed by the Board of Superintendence for a maximum period of three years. Its members currently are:

- Mario M. Busso, President of the Board of Statutory Auditors
- Rodolfo Molinuevo Orue
- Pierluigi Bernasconi

The Board of Statutory Auditors reports to the Board of Superintendence. It is responsible for the internal audit of the IOR's books on a quarterly basis. In addition, the Board of Statutory Auditors reviews the annual financial statements.

The **Directorate**, appointed by the Board of Superintendence and approved by the Commission of Cardinals, is responsible for the operational activities of the Institute and is accountable to the Board of Superintendence.

**Rolando Marranci**
*General Director*

In 2014, Rolando Marranci was sole General Director. On 6 March 2015, Gian Franco Mammì was appointed Vice Director.

CHAPTER 7
# Regulatory Framework and Tax Requirements



## a) Regulatory framework

The IOR is subject to the legislation and regulatory framework of the Holy See and the Vatican City State.

In particular, the Vatican legal framework recognises Canon Law as the primary source of legislation and the primary criterion for its interpretation. Alongside this, there are six organic laws and other ordinary laws specific to the Vatican City State. As regards matters not covered by Vatican laws, laws and other regulations issued by the Italian Republic are observed as supplementary, if transposed by the competent Vatican authority. They are adopted on condition that they do not contravene the precepts of divine law, the general principles of Canon Law or the provisions of the Lateran Pact and subsequent Agreements, and provided that they are applicable in relation to the state of affairs existing in the Vatican City. (See law n. LXXI on the source of law, promulgated by Pope Benedetto XVI on 1 October 2008).

According to article 1.4 of n. LXXI on the sources of law, the legal framework also conforms to the general norms of international law, and to those derived from treaties and other accords of which the Holy See is part.

As noted, the Istituto per le Opere di Religione is supervised by the Financial Intelligence Authority (AIF), the financial regulatory body for the Vatican City State. In this regard, law n. XVIII of 2013 clarifies and consolidates AIFs functions, powers, and responsibilities in the exercise of its supervisory and regulatory tasks, with the purpose of preventing and countering money laundering and the financing of terrorism, the exercise of financial information functions, as well as financial supervisory functions, as established by Pope Francesco in the Motu Proprio of 8 August 2013.

With regard to the context of supervision, following the implementation of Vatican City State Law n. XVIII, which covers norms of transparency, financial supervision, and information, AIF issued Regulation 1 / 2015 (the “Regulation”) (“Prudential Supervision of the Entities Carrying out financial activities on a professional basis”).

The Regulation stipulates the criteria for the organisation and management of entities carrying out authorised financial activities on a professional basis, stipulating among other things the structure of the entity, the organisation of administrative and treasury functions, the policies, procedures, and mechanisms of internal control, and the policies and procedures of management.

In order for the Institute to be compliant with the provisions of the Regulation, specific work streams have been put in place to allow for full compliance with the provisions of the Regulation by no later than 13 January 2016, the final date for complete compliance as required by article 121.3 of the regulation (Titled “Transition Period”).

Ahead of the issue of new regulations on the preparation and publication of the financial statements, which will be applied to the upcoming 2015 financial statements, it is noted that the Financial statements here presented have been prepared in conformity with those in the past, applying generally accepted accounting standards, as required by the current Statutes.

In this regard, International Accounting Standards (IAS-IFRS) were adopted.
Furthermore, Financial Risk Management disclosures were consistent with those used in the previous financial statements, being within the transitory period ahead of the full compliance with the Vatican framework regarding prudential supervision.

In consequence, beginning with the Annual Report 2015, the information provided to clients and the public will be compiled and integrated in a manner that complies with the new Regulation to be issued.

### b) Tax requirements

Over the past year, the IOR has engaged in revising its tax requirements related to its activities and customers. Starting in 2015, the IOR will be subject to the Foreign Account Tax Compliance Act (FATCA), a United States federal law that requires U.S. persons, including individuals who live outside the United States, to report their financial accounts held outside of the United States to the U.S. Internal Revenue Service (“IRS”).

FATCA also requires foreign financial institutions to report to the IRS about the accounts of their U.S. clients. In this context, the Holy See has reached an agreement in substance with the United States on the terms of an IGA (Intergovernmental Agreement). Therefore at the present time the Holy See is a jurisdiction treated by the US Authorities as if it had an IGA in effect as of 30 November 2014. As a consequence, the IOR has been assigned an identification code (GIIN) from the Internal Revenue Service (IRS). The IOR does not see any matter that might prevent it from fully complying with the obligations arising from the IGA.

The IOR has also been working to review and confirm its tax position and that of its customers towards countries with which they have investment relationships. This work has identified probable contingencies which relate to prior years as a result of different interpretations regarding the legal nature of the Institute and the consequent related tax treatments. At this stage no reliable estimate can be made. As a consequence, under the provision of IAS 37 par. 26, no specific provision has been accounted for in the 2014 Financial Statements. However, the IOR remains fully committed to addressing any incorrect treatment with the relevant tax authorities having the capacity to meet any payments that may arise from the above review.

CHAPTER 8

# Report of the Commission of Cardinals



The Commission of Cardinals discharged the duties incumbent upon it under the law and the Statutes of the IOR in the year under review. It was notified of all major events. The Secretary of the Commission of Cardinals, the Prelate, regularly participated in the meetings of the Board of Superintendence, and so too sometimes did the President of the Commission, in order to get direct information from the members of the board.

The Commission of Cardinals wishes to thank the Board of Superintendence and the employees of the IOR for the work they have done during the year under review.

CHAPTER 9

# Report of the Board of Superintendence

In 2014, the Board of Superintendence met on a regular basis, once together with the Commission of Cardinals. The Prelate attended as well.

It approved the Financial Statements for 2013 provided by the Directorate and audited by Deloitte & Touche S.p.A., and submitted them to the Commission of Cardinals. It supervised the Institute's operational and financial performance continuously throughout the year and approved the budget for 2015.

The Board of Superintendence focused in particular on the reform process of the Institute, the compliance of the Institute with Vatican City State and international laws, including the recommendations by Moneyval. It closely supervised the anti-money laundering and remediation efforts undertaken by the Institute as well as the investigation of legacy cases.

The Board of Superintendence appointed Deloitte & Touche S.p.A. as auditor of the financial statements for 2014.

CHAPTER 10

# Financial Statements

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## SECTION I

### BALANCE SHEET AS OF 31 DECEMBER 2014

| | *Notes* | *2014* | *2013* |
|---|---|---|---|
| | | *EUR 000* | *EUR 000* |
| **ASSETS** | | | |
| Cash and Bank deposits | 1 | 567,358 | 715,990 |
| Trading securities | 2 | 1,718,136 | 1,748,901 |
| Gold, medals and precious coins | 3 | 33,208 | 29,867 |
| Derivative financial instruments | 4 | – | – |
| Loans and advances to customers | 5 | 22,408 | 29,462 |
| Loans and receivables securities | 6 | 187,677 | 250,870 |
| Investment securities, equities available for sale | 7 | 10,390 | 13,930 |
| Held to maturity securities | 8 | 645,054 | 574,816 |
| Investment in subsidiaries | 9 | 15,835 | 15,835 |
| Investment properties | 10 | 2,181 | 2,126 |
| Equipment and furnishings | 11a | 123 | 202 |
| Intangible assets | 11b | 833 | 1,099 |
| Other assets | 12 | 7,572 | 7,919 |
| **Total Assets** | | **3,210,775** | **3,391,017** |
| **LIABILITIES** | | | |
| Due to banks | 13 | 16 | 1 |
| Due to depositors | 14 | 2,361,863 | 2,544,278 |
| Derivative financial instruments | 4 | – | – |
| Other liabilities | 15 | 29,955 | 36,520 |
| Post-employment benefit plans | 16 | 123,947 | 90,171 |
| **Total Liabilities** | | 2,515,781 | 2,670,970 |
| **EQUITY** | | | |
| Equity reserves | | 309,874 | 309,874 |
| Retained earnings reserve | | 357,426 | 409,561 |
| Fair Value reserve investment securities, equities available for sale | | – | 5,368 |
| Post-employment benefit actuarial gain (loss) reserve | | (41,639) | (7,621) |
| Net profit for the year | | 69,333 | 2,865 |
| **Total Equity** | | 694,994 | 720,047 |
| **Total Liabilities and Equity** | | **3,210,775** | **3,391,017** |

The notes on each item are disclosed in Section IV “Explanatory notes to the financial statements”. For the details of Equity items, please refer to “Statement of changes in equity” in Section I.

## INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2014

| | *Notes* | *2014* | *2013* |
|---|---|---|---|
| | | *EUR 000* | *EUR 000* |
| Interest income | 17 | 61,088 | 76,356 |
| Interest expense | 17 | (10,428) | (22,544) |
| **Net interest result** | | 50,660 | 53,812 |
| Fee and commission income | 18 | 16,666 | 17,591 |
| Fee and commission expense | 18 | (2,304) | (3,481) |
| **Net fee and commission result** | | 14,362 | 14,110 |
| Dividend income | 19 | 2,781 | 3,796 |
| Net trading result | 20 | 36,717 | (16,545) |
| **Operating result** | | **104,520** | **55,173** |
| Operating expenses | 21 | (28,880) | (32,187) |
| **Net operating result** | | **75,640** | **22,986** |
| Impairment losses | 23 | (7,157) | (5,725) |
| Other net income (expense) | 22 | 850 | (14,396) |
| **Net profit for the year** | | **69,333** | **2,865** |

The notes on each item are disclosed in Section IV of these financial statements. The item Other net income (expense) was reclassified under the line Net operating result for the sake of clarity.

## STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2014

| | *Notes* | *2014* | *2013* |
|---|---|---|---|
| | | *EUR 000* | *EUR 000* |
| **Net profit for the year** | | **69,333** | **2,865** |
| **Items that may be reclassified subsequently to Income Statement** | | | |
| Net fair value gain (loss) on available for sale investment securities | 7 | – | 5,368 |
| Reversal of FV loss on AFS securities at Impairment loss into Income Statement | 7 | – | – |
| Reversal to reserve of fair value gain (loss) on available for sale investment securities recorded in the prior years | 7 | (5,368) | – |
| **Items never reclassified subsequently to Income Statement** | | | |
| Post-employment benefit actuarial gain (loss) of the year | 16 | (34,018) | (2,745) |
| **Total Comprehensive Income** | | **29,947** | **5,488** |

The notes are disclosed in Section IV of these financial statements.

## CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2014

| *Direct Method* | | *Notes* | *2014* | *2013* |
|---|---|---|---|---|
| | | | *EUR 000* | *EUR 000* |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | | |
| Interest, fees and commissions received | | | 79,988 | 101,607 |
| Interest, fees and commissions paid | | | (17,012) | (36,758) |
| Dividend received | | | 2,781 | 3,796 |
| Realised Net trading result | | | 27,381 | 18,293 |
| Other income (expense) | | | 498 | (14,951) |
| Cash payments to employees and suppliers | | | (28,528) | (31,086) |
| | | | 65,108 | 40,901 |
| **CHANGES IN OPERATING ASSETS AND LIABILITIES** | | | | |
| Net (increase) or decrease in trading securities and derivatives | | | 38,541 | 948,635 |
| Net (increase) or decrease in gold, medals and precious coins | | | (2,760) | 53 |
| Net (increase) or decrease in term deposits with banks | | | (62,000) | 85,171 |
| Net (increase) or decrease in loans and advances to customers | | | 4,098 | (8,761) |
| Net (increase) or decrease in other assets | | | 347 | 51,399 |
| Net increase or (decrease) in due to banks | | | 15 | (2) |
| Net increase or (decrease) in due to depositors | | | (178,135) | (1,548,462) |
| Net increase or (decrease) in other liabilities | | | (7,971) | 10,396 |
| Net cash from operating activities | A | | (142,757) | (420,670) |
| **CASH FLOWS GENERATED – USED IN INVESTING ACTIVITIES** | | | | |
| Purchase of furnishings and equipment | | 11a | (15) | (171) |
| Disposal of furnishings and equipment | | 11a | – | 26 |
| Purchase of intangible assets | | 11b | (235) | (1,155) |
| Improvements of real estate properties | | 10 | (73) | – |
| Purchase of investment securities AFS | | 7 | (6,321) | – |
| Disposal of investment securities AFS | | 7 | 2,432 | 1,214 |
| Purchase of HTM or L&R securities | | 6,8 | (174,061) | (139,337) |
| Disposal of HTM or L&R securities | | 6,8 | 173,084 | 193,183 |
| Net cash from (used in) investing activities | B | | (5,189) | 53,760 |
| **CASH FLOWS USED IN FINANCING ACTIVITIES** | | | | |
| Distribution of prior year profits | C | | (55,000) | (54,700) |
| Forex effects | D | | (9,403) | 3,510 |
| Net increase (decrease) in cash and cash equivalents | (A+B+C+D) | | (212,349) | (418,100) |
| Cash and cash equivalents at beginning of the year | | | 692,981 | 1,111,081 |
| **Cash and cash equivalents at the end of the year** | | 1 | **480,632** | **692,981** |

The notes are disclosed in Section IV of these financial statements.

## STATEMENT OF CHANGES IN EQUITY

| | | *Comprehensive Income* | | | | |
|---|---|---|---|---|---|---|
| | *Equity reserves* | *Fair value reserve investment securities Available for sale* | *Post employment benefit actuarial gain (loss) reserve* | *Net profits* | *Retained earnings reserve* | *Total* |
| | *EUR 000* | *EUR 000* | *EUR 000* | *EUR 000* | *EUR 000* | *EUR 000* |
| **Balance at 31 December 2012 / 1 January 2013** | **309,874** | **–** | **(4,876)** | **86,615** | **377,646** | **769,259** |
| Distribution according the indications of Commission of Cardinals | – | – | – | (54,700) | – | (54,700) |
| Transfer from retained earnings reserve | – | – | – | (31,915) | 31,915 | – |
| Net fair value gain (loss) on available for sale investment securities (note 7) | – | 5,368 | – | – | – | 5,368 |
| Post-employment benefit actuarial gain (loss) of the year | – | – | (2,745) | | | (2,745) |
| Total other comprehensive income | – | 5,368 | (2,745) | – | – | 2,623 |
| Net profit for the year 2013 | – | – | | 2,865 | – | 2,865 |
| Total comprehensive income 2013 | – | 5,368 | (2,745) | 2,865 | – | 5,488 |
| **Balance at 31 December 2013 / 1 January 2014** | **309,874** | **5,368** | **(7,621)** | **2,865** | **409,561** | **720,047** |
| Distribution according the indications of Commission of Cardinals | – | – | – | (55,000) | – | (55,000) |
| Transfer to retained earnings reserve | – | – | – | 52,135 | (52,135) | – |
| Reversal to reserve of fair value gain (loss) on available for sale investment securities recorded in the prior years | | (5,368) | | | | (5,368) |
| Net fair value gain (loss) on available for sale investment securities (note 7) | – | – | – | – | – | – |
| Post-employment benefit actuarial gain (loss) of the year | | – | (34,018) | – | – | (34,018) |
| Total other comprehensive income | – | (5,368) | (34,018) | – | – | (39,386) |
| Net profit for the year 2014 | – | – | | 69,333 | – | 69,333 |
| Total comprehensive income 2014 | – | (5,368) | (34,018) | 69,333 | – | 29,947 |
| **Balance at 31 December 2014** | **309,874** | **–** | **(41,639)** | **69,333** | **357,426** | **694,994** |

The notes are disclosed in Section IV of these financial statements.

SECTION II



# General information and summary of significant accounting policies

## General information

The financial statements of the Institute were prepared by the Directorate and approved by the Board of Superintendence, which transmits it to the Commission of Cardinals.

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

## Accounting policies

### A) BASIS OF PREPARATION

The IOR's financial statements have been prepared in accordance with International Financial Reporting Standards (IAS / IFRS) as issued by the International Accounting Standards Board. This annual report is a separate financial statement.

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

Disclosures under IFRS 7 "Financial Instruments, disclosures" about the nature and extent of risks, and Capital Disclosures under IAS 1 "Presentation of Financial Statements", have been included in Section V under "Financial risk management". The principal accounting policies applied in the preparation of these financial statements are detailed below. These policies are consistent with those of the previous financial year, except for new standards, new interpretations, or amendments of standards.

The Institute adopted the IFRS 10 "Consolidated Financial Statements", IFRS 11 "Joint arrangements", IFRS 12 "Disclosure of interests in other entities", and IFRS 13 "Fair value measurement", as of 1 January 2013. The financial statements of the Istituto per le Opere di Religione are prepared in Euro. Unless otherwise stated, all amounts are given in thousand Euro. For all items, the values calculated in the year 2014 and the corresponding values for the previous year are given. Where necessary, the comparative figures have been adjusted to conform to changes in presentations in the current year.

In preparing financial statements, the IOR is presumed to be a going concern. On the date the Board of Superintendence approved the financial statements, there were no material uncertainties and therefore no significant doubt regarding the Institute's ability to continue as a going concern for the foreseeable future in accordance with IAS 1 "Presentation of Financial Statements". The financial statements fairly present the financial position, financial performance, and cash flows of the Institute. The preparation of IFRS-compliant financial statements requires the Directorate to make a large

number of estimates and assumptions with regard to the future that may, naturally, not coincide with actual future conditions. Estimates and assumptions affect the reported amounts of certain assets, liabilities, revenues and expenses. In addition, changes in assumptions may have a significant impact on the financial statements from the period during which the assumptions changed. The preparation of IFRS-compliant financial statements also requires the Directorate to exercise judgements in applying the IOR's accounting policies to estimate the carrying value of assets and liabilities not readily obtainable from other sources.

The Directorate believes that the underlying assumptions are appropriate and that the IOR's financial statements fairly present the financial position and results. All estimates are based on historical experience and /or expectations with regard to future events that seem reasonable under the given circumstances. They are also reassessed on a regular basis. Those areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Section III "Critical accounting estimates and judgments". The financial statements do not recognise tax provisions because no corporate income tax exists in Vatican City State.

The Institute, despite holding a 100 % stake in SGIR, does not prepare consolidated financial statements, because the additional information coming from the consolidated financial statements is largely irrelevant, in the context of the IAS Framework. The financial statements for the subsidiary are insignificant compared with those of the IOR and thus a consolidated financial statement would not materially differ from the financial statements here presented. The Institute provides the additional information required by the standard IFRS 12 "Disclosure of interests in other entities". This standard lists the information to provide in the financial statements related to the investments in unconsolidated structured entities.

After year-end there were no significant events that would require adjustments to the 2014 financial statements.

## B) IMPACT OF NEW ACCOUNTING PRONOUNCEMENTS, NEW STANDARDS, INTERPRETATIONS AND AMENDMENTS TO PUBLISHED STANDARDS

### b1) Impact of New Accounting Pronouncements, new Standards, interpretations and amendments to published standards effective from 1 January 2013 and relevant to the IOR's accounting

**IFRS 10 – IFRS 12 – IAS 27 (Amendments)** (October 2012) "Investment Entities" (effective 1 January 2014).

The amendments introduce an exception to the consolidation of subsidiaries for an investment company, with the exception of cases in which the subsidiaries provide services that relate to the investment activities of such companies. Pursuant to these amendments, an investment company must evaluate its investments in subsidiaries at fair value. The Institute adopted the amendment from 1 January 2014 but there has been no impact on the accounts.

**IAS 32 (Amendment)** (December 2011) "Offsetting financial assets and liabilities" (effective 1 January 2014). The amendment clarifies the application of certain criteria for offsetting financial assets and financial liabilities on the balance sheet. The Institute adopted IAS 32 from 1 January 2014 but there has been no impact on the accounts.

**IAS 36 (Amendment)** (May 2013) "Recoverable amount disclosures for non-financial assets" (effective 1 January 2014). The amendment clarifies that the additional information to be provided about the recoverable amount of the assets (including goodwill) or cash-generating unit, in the event that their recoverable amount is based on fair value less costs of disposal, concerns only assets or cash-generating units to which a loss in value was recognised or reversed during the financial year. The Institute adopted IAS 36 from January 1 2014 but there has been no impact on the accounts.

**IAS 39 (Amendment)** (June 2013) "Financial instruments: Recognition and measurement – Novation of derivatives and continuation of hedge accounting" (effective 1 January 2014). The changes include the introduction of certain exemptions from the requirements of hedge accounting as defined by IAS 39, when an existing derivative needs to be replaced with a new derivative having, by law or regulation, directly (or indirectly), a central counterparty (Central Counterparty – CCP). The Institute adopted IAS 39 from 1 January 2014 but there has been no impact on the accounts.

**b2) Standards, interpretations and amendments to published standards effective 1 January 2014 that are not relevant to the IOR**

**IFRIC 21** (May 2013) "Levies" (effective 1 January 2014). Liability should only be recognised in interim reports once the event giving rise to the liability has occurred.

**b3) Standards, interpretations and amendments to published standards relevant to the IOR's accounting that are not yet effective and that have not been early applied**

The following new standards and interpretations of existing standards have been published and are mandatory for the IOR's accounting periods beginning on or after 1 January 2015 but the IOR has not early adopted them.

**IFRS 9 (New Standard)** (July 2014) "Financial Instruments: Classification and Measurement – Financial Assets" (effective 1 January 2018). The new standard uses a single approach based on the management of financial instruments and the contractual cash flow characteristics of the financial assets to determine the evaluation criteria, replacing the many different rules in IAS 39. The main change concerns the accounting treatment of changes in fair value of a financial liability designated as financial liability at fair value through profit or loss, if these variations are due to changes in the creditworthiness of the issuer of the liability. Under the new standard, these changes must be recognised in "Other comprehensive income" and not in the Income Statement. With reference to the impairment model, the new standard requires that the estimate of loan losses to be is made on the basis of the model of expected losses (and not on the model of incurred losses), using information supportable, available without unreasonable effort or expense, that includes historical data current and prospective. The standard requires that the impairment model applies to all financial instruments and to financial assets carried at amortised cost, to financial assets measured at fair value through other comprehensive income, to receivables arising from lease and to trade receivables. The standard introduces a new model of hedge accounting in order to adapt the requirements of the current IAS 39,

which sometimes were considered too stringent and not suited to reflecting the risk management policies of the company. Under the new regulations an entity applying the fair value option to measure its financial liabilities can no longer recognise within the Income Statement any fair value changes related to its own credit risk, but must instead recognise them without effect on Income Statement under Other Comprehensive Income and therefore directly in Equity. The Institute will adopt IFRS 9 from 1 January 2018 and it believes that there will be a significant impact on the IOR's financial statements. The IOR has not yet finalised the assessment of the financial impact.

**IFRS 11 (Amendment)** (May 2014) "Accounting for Acquisitions of Interests in Joint Operations" (effective 1 January 2016). The Amendments provide guidance on how to account for the acquisition of an interest in a joint operation. The Institute will adopt the amendment to IFRS 11 from 1 January 2016.

**IFRS 15 (New Standard)** (May 2014) "Revenue from Contracts with Customers" (effective 1 January 2017). The new standard establishes a new model for revenue recognition, which will apply to all contracts, insurance contracts and financial instruments with customers except for contracts related to other standards IAS / IFRS (for example leasing). The basic steps for the recognition of revenue under the new model are: identification of the contract with the customer; the identification of performance obligations of the contract; pricing; the allocation of the price to the performance obligations of the contract; the criteria for inclusion of revenue when the entity satisfies each performance obligation. The Institute will adopt the amendment to IFRS 15 from 1 January 2017.

**IFRS 10 – IAS 28 (Amendments)** (September 2014) "Sale or Contribution of Assets between an Investor and its Associate or Joint Venture" (effective 1 January 2016). The Amendments provide that when a sale transfer of assets to a subsidiary or joint venture occurs, the measure of profit or loss is related to the assets transferred, whether or not they constitute a business recognised in the balance sheet of the assignor, as defined by IFRS 3. In the event that the assets or the subsidiary sold / transferred represent a business, the entity shall recognise the gain or loss on the entire investment held. If not, the entity shall discard the portion of profit or loss related to the share still held by the entity. The Institute will adopt the amendment from 1 January 2016.

"Annual Improvements to IFRSs: 2010 – 2012 Cycle" (Amendment) (December 2013) (effective 1 July 2014); the document incorporates the changes to the standards as part of the annual process of improvement. The main changes include:

**IFRS 2** Share Based Payments – Definition of vesting condition. Some changes are made to the definitions of "vesting condition" and "market condition" and added further definitions of "performance conditions" and "service condition" (previously included in the definition of "vesting condition").

**IFRS 3** Business Combinations – Accounting for contingent consideration. The amendment clarifies that a contingent consideration under business combination classified as an asset or a financial liability shall be remeasured at fair value at each balance sheet date of the accounting period, and changes in fair value are recognised in the Income Statement or between elements of comprehensive income on the basis of the requirements of IAS 39 (or IFRS 9).

**IFRS 8** Operating segments – Aggregation of operating segments. The changes require an entity to provide information regarding the assessments made by management in the application of the criteria for aggregation of operating segments, including a description of the operating segments and aggregate economic indicators considered in determining whether these operating segments have similar economic characteristics.

**IFRS 8** Operating segments – Reconciliation of total of the reportable segments' assets to the entity's assets. The amendments clarify that the reconciliation between the total assets of the operating segments and the total assets of the entity as a whole must be made if the total assets of the operating segments are regularly reviewed by the chief operating decision maker operating entity.

**IFRS 13** Fair Value Measurement – Short-term receivables and Payables. The Basis for Conclusions of this principle have been modified in order to clarify that with the issuance of IFRS 13, and resulting amendments to IAS 39 and IFRS 9, the possibility of accounting for receivables and trade payables without detecting the effects of an update remains valid, if these effects are not material.

**IAS 16** "Property, plant and equipment" and IAS 38 "Intangible Assets – Revaluation method: proportionate restatement of accumulated depreciation / amortisation". The changes eliminate the inconsistencies in the recognition of depreciation when a tangible asset or intangible asset is revalued. The new requirements specify that the gross carrying value must be consistent with the post-revaluation carrying value of the asset, and that the accumulated depreciation must be equal to the difference between the carrying value and the gross carrying amount, net of losses to the posted values.

**IAS 24** "Related Party Disclosures – key management personnel." This clarifies that when the services of key management personnel are provided by an entity (and not a natural person), this entity should be regarded as a related party.

The Institute will adopt the amendments from 1 January 2015.

"Annual Improvements to IFRSs: 2011 – 2013 Cycle" (Amendment) (December 2013) (effective 1 July 2014); the document incorporates the changes to the standards as part of the annual process of improvement. The main changes include:

**IFRS 3** Business Combinations – Scope exception for joint ventures. The amendment states that paragraph 2 (a) of IFRS 3 excludes from the scope of IFRS 3 the formation of all types of joint arrangement, as defined by IFRS 11.

**IFRS 13** Fair Value Measurement – Scope of portfolio exception (para. 52). The amendment clarifies that the portfolio exception included in paragraph 52 of IFRS 13 applies to all contracts included within the scope of IAS 39 (or IFRS 9) regardless of whether they meet the definition of financial assets and liabilities provided by IAS 32.

**IAS 40** Investment Properties – interrelationship between IFRS 3 and IAS 40. The amendment clarifies that IFRS 3 and IAS 40 are not mutually exclusive and that, in order to determine whether the purchase of a property falls within the scope of IFRS 3 and IAS 40, it is necessary to refer respectively to the specific guidance provided by IFRS 3 or IAS 40.

The Institute will adopt the amendments from 1 January 2015.

Annual Improvements to IFRSs: 2012 – 2014 Cycle (Amendment) (September 2014) (effective 1 January 2016); the document incorporates the changes to the standards as part of the annual process of improvement. The main changes include:

**IFRS 5** "Non-current Assets Held for Sale and Discontinued Operations – Changes in methods of disposal." The amendment introduces specific guidance to IFRS 5 in case an entity reclassifies an asset (or disposal group) from the category held-for-sale to the category held-for-distribution (or vice versa), or when requirements to classify an asset as held-for-distribution decay.

**IFRS 7** "Financial Instruments: Disclosure. Servicing contracts." The document regulates the introduction of additional guidance to clarify whether a servicing contract constitutes a continuing involvement in a transferred asset for the purposes of the request in relation to the assets transferred.

**IAS 19** "Employee Benefits – Discount rate: regional market issue." The amendment clarifies that the high quality corporate bonds used to determine the discount rate of post-employment benefits should be issued in the same currency used for payment of benefits. The amendments clarify that the breadth of the market for high quality corporate bonds to be considered is the level of the reference currency used.

**IAS 34** "Interim Financial Reporting – Disclosure of Information" elsewhere in the interim report. The document introduces changes in order to clarify the requirements in the event that the information required is presented in the interim financial report but outside the interim financial statements. The amendment specifies that such information is included through a cross-reference from the interim financial statements to other parts of the interim financial report and that the document is available to readers of the financial statements in the same manner and with the same time of the interim financial statement.

The Institute will adopt the amendments from 1 January 2016.

**IAS 1 (Amendment)** (December 2014) "Disclosure Initiative" (effective 1 January 2016).
The purpose of the amendment is to clarify the elements of information that may be perceived as representing impediments to a clear and intelligible preparation of financial statements. The changes are as follows:

- Materiality and aggregation: it is clear that a company should not obscure information by aggregation or disaggregation, and that the materiality should be applied to the financial statements, notes and specific disclosure requirements of IFRS.
  The disclosures required by IFRS must be provided only if the information is material.

- Statement of financial statement and statement of comprehensive income: clarifies that the list of entries specified by IAS 1 for these tables can be disaggregated and aggregated as appropriate. Also includes a guideline on the use of subtotals in statements.

- Presentation of items of other comprehensive income ("OCI"): clarifies that the share of OCI of associates and joint ventures accounted for using the equity method must be presented in aggregate in a single voice, in turn divided between those components subject to future reclassifications to the income statement, and those that are not.

- Notes: clarifies that entities have flexibility defining the structure of the notes and provides guidance on how to set up a systematic order of the notes.



The Institute will adopt the amendments to IAS 1 from 1 January 2016.

**IAS 16 (Amendment)** (May 2014) “Property, plant and Equipment – Clarification of acceptable methods of depreciation and amortisation” (effective 1 January 2016). The amendment states that the criteria for depreciation determined according to the revenues are not appropriate; the revenue generated by an activity that includes the use of amortisation generally reflect factors other than just consumption of economic benefits of the asset. The Institute will adopt the amendment IAS 16 from 1 January 2016.

**IAS 38 (Amendment)** (May 2014) “Intangible Assets – Clarification of acceptable methods of depreciation and amortisation” (effective 1 January 2016). The amendment introduces a rebuttable presumption, that a depreciation method based on revenues is considered generally inappropriate for the same reasons set out by the amendments made to IAS 16. In the case of intangible assets, however, this presumption can be overcome, but only in limited and specific circumstances. The Institute will adopt the amendment to IAS 38 from 1 January 2016.

**IAS 19 (Amendment)** (November 2013) “Employee Benefits plans: employee contributions” (effective 1 July 2014). The amendment proposes to submit contributions (relating only to the service provided by the employee during the year) made by employees or third parties to defined benefit plans to reduce the service cost for the year in which the contribution is paid. The necessity of such a proposal has arisen with the introduction of the new IAS 19 (2011), where it is believed that such contributions are to be interpreted as part of a post-employment benefit, rather than a benefit of the short term and, therefore, that this contribution is to be spread over the years of service of the employee. The Institute will adopt the amendment to IAS 19 from 1 January 2015.

**IAS 27 (Amendment)** (August 2014) “Equity Method in Separate Financial Statements” (effective 1 January 2016). The amendment introduces, in separate financial statements, the option to use the equity method for the evaluation of investments in subsidiaries, jointly controlled entities and associates. Consequently, following the introduction an entity can detect these investments in the separate financial statements: at cost; as required by IFRS 9 (or IAS 39); using the equity method. The Institute will adopt the amendment to IAS 27 from 1 January 2016.

**b4) Standards, interpretations and amendments to published standards that are not yet effective and that are not relevant to the IOR’s accounting.**

**IFRS 14 (New standard)** (January 2014) “Regulatory Deferral Accounts” (effective 1 January 2016).

**IAS 41 (Amendment)** (June 2014) “Agriculture – Bearer Plants” (effective 1 January 2016).

**IFRS 1** (December 2013) “First-time Adoption of International Financial Reporting Standards – Meaning of “effective IFRS” (effective 1 July 2014).

**IFRS 2** (December 2013) “Share Based Payments – Definition of vesting condition” (effective 1 July 2014).

**IFRS 3** (December 2013) "Business Combination – Accounting for contingent consideration" (effective 1 July 2014).

**IFRS 3** (December 2013) "Business Combinations – Scope exception for joint ventures" (effective 1 July 2014).

**IFRS 8** (December 2013) "Operating segments – Aggregation of operating segments" (effective 1 July 2014).

**IFRS 8** (December 2013) "Operating segments – Reconciliation of total of the reportable segments' assets to the entity's assets" (effective 1 July 2014).

**IFRS 13** (December 2013) "Fair Value Measurement – Scope of portfolio exception" (effective 1 July 2014).

**IAS 40** (December 2013) "Investment Properties – Interrelationship between IFRS 3 and IAS 40" (effective 1 July 2014).

## C) FOREIGN CURRENCY CONVERSION

**c1) Functional and presentation currency**

The functional currency is the currency in which the items included in the financial statements must be measured. According to IAS 21 "The effects of changes in foreign exchange rates" the functional currency is the currency of the primary economic environment in which the entity operates. This is the currency that determines the pricing of transactions, but it is not necessarily the currency in which transactions are denominated. The presentation currency is the currency in which the financial statements are presented. IAS 21 allows an entity to present its financial statements in any currency. The IOR's functional and presentational currency is the Euro, which is the currency of the primary economic environment in which the Institute operates. In fact, the Euro is the currency in which the majority of the funds are received and in which the funds are invested.

**c2) Transactions and balances**

Foreign currency transactions, if they impact profit or loss accounts, are converted into the functional currency using the exchange rates applicable at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are converted into the functional currency using the spot exchange rate at the reporting date (closing rate). Non-monetary assets and liabilities denominated in foreign currencies are translated using the rate at the date their amount (cost or fair value) was determined. Non-monetary items carried at cost are converted using the initial recognition rate. Non-monetary items carried at fair value are translated using the rate at the date their fair value was measured. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the conversion at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Income Statement as item "Net trading result", line "Foreign Exchange".

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



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

## D) CASH AND CASH EQUIVALENTS

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash, non-restricted balances with central banks and bank deposits, including loans and advances to banks.

## E) FINANCIAL ASSETS

The IOR classifies its financial assets into the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. The Directorate determines the classification of its investments at the time of initial recognition, considering also the nature and purpose of the financial assets. All financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the IOR has substantially transferred all risks and rewards of ownership. Sales of financial assets are recognised on the trade date, which is the date on which the IOR commits to selling the asset. Initial recognition and subsequent measurement criteria change according to the relevant category.

**e1) Financial assets at fair value through profit or loss (FVTPL).**
A financial asset is classified under this category if acquired principally for the purpose of selling in the short term or if the management designates it as at FVTPL. This category contains financial assets held for trading, which are reported under "Trading securities". Derivatives are also categorised as held for trading unless they are designated as hedging instruments. Purchases of financial assets at fair value through profit or loss are recognised on the trade date which is the date on which the IOR commits to purchasing the asset. Financial assets at fair value through profit or loss are initially recognised at fair value, which generally corresponds to the initial cash consideration – without adding direct transaction costs. For the subsequent measurements, the financial assets FVTPL are carried at fair value, with any gains or losses arising on remeasurement recognised in the Income Statement. Gains and losses arising from changes in the fair value of the financial assets FVTPL category are included in the item "Net trading result" in the period in which they arise. Realised gains and losses coming from sales or reimbursement of the financial assets FVTPL are also included in the same item. The accounting policies affecting any dividend or interest earned on the financial assets FVTPL are disclosed later in the current section, in notes r and t. The accounting policies affecting derivatives held for trading are disclosed in the current section, in note g. For the measurement of fair value, the IOR adopted the IFRS 7 amendment and then successively the changes introduced in IFRS 13 which defines a fair value hierarchy according to the parameters used.

The financial activities are thus classified according to the following hierarchy.

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities, i.e. those that are readily available in the market and are normally obtainable from multiple sources.
Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
Level 3: Inputs for assets or liabilities that are not based on observable market data (unobservable inputs).

For further information about how the IOR classifies the financial assets measured at fair value, refer to Section IV note 27.

**e2) Loans and receivables**
"Loans and receivables" are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

They arise:

a) when the IOR provides money, securities, goods or services directly to a debtor with no intention of trading the receivable;
b) when the IOR purchases loans and receivables debt securities offered through private placements, that the Institute did not designate as at fair value through profit or loss or available for sale financial assets. These financial assets are subject to the risk of the credit deterioration of the counterparty.

Loans are recognised when cash is advanced to the borrower.

They are initially recognised at fair value, which is the cash given to originate the loan, plus any direct transaction costs. Loans are subsequently measured at amortised cost using the effective interest rate method.

Securities "Loans and receivables" are initially recognised on the trade date, which is the date on which the IOR commits to purchasing the asset. They are initially recognised at fair value plus any direct transaction costs. Securities "Loans and receivables" are subsequently measured at amortised cost using the effective interest rate method. They may also be impaired under the circumstances disclosed in current Section note u. A gain or loss on "Loans and receivables" is recognised in the Income Statement through the financial amortisation (item "Interest income / expense").

When the assets are removed they are recognised under "Other net income (expense)":

- "Losses on advances" for loans;
- "Gains / losses on disposal of loans and receivables securities" for securities.

When impairment losses are recognised under "Impairment losses":

- "Impairment losses on loans and advances" for loans;
- "Impairment losses on loans and receivables securities" for securities.

The accounting policies affecting any interest earned on the financial assets “Loans and receivables” are set out later in note r. For the rules applied to the impairment of financial assets pertaining to the category “Loans and receivables”, refer to note u of the present Section.



**e3) Held to maturity financial assets**

“Held to maturity” investments are quoted non-derivative financial assets with fixed or determinable payments and with fixed maturities which the IOR has the intention and ability to hold to maturity. If the IOR sells more than an insignificant amount of “Held to maturity” assets, the entire category would be reclassified as available for sale and for the following two years no financial asset can be classified in this category. Securities “Held to maturity” are also initially recognised on the trade date, which is the date on which the IOR commits to purchasing the asset. They are initially recognised at fair value plus any direct transaction costs. Securities “Held to maturity” are subsequently measured at amortised cost using the effective interest rate method. They may also be impaired under the circumstances disclosed in the current Section, note u. Gains and losses on “Held to maturity” financial assets are recognised in the Income Statement through the financial amortisation (item “Interest income”) or when the assets are removed (item “Other net income (expense)” line “Gains / losses on held to maturity securities”) or when impairment losses are recognised (item “Impairment losses” line “Impairment losses on held to maturity secu-rities”). The accounting policies affecting any interest earned on the financial assets “Held to maturity” are disclosed later in the current Section (note r). For the rules applied to the impairment of financial assets pertaining to the category “Held to maturity”, refer to note u in the present Section.

**e4) Available for sale financial assets**

“Available for sale” investments are those intended to be held for an indefinite period of time, also because of agreements that limit disposal for a certain time. In addition, “Available for sale” financial assets are those non derivative financial assets that are not classified as held for trading or loans and receivables or held to maturity investments or financial assets at fair value through profit or loss. This category contains financial assets held for investment, which are reported under “Investment Securities, equities Available for sale”. Securities “Available for sale” are also initially recognised on the trade date, which is the date on which the IOR commits to purchasing the asset. They are initially recognised at fair value plus any direct transaction costs. “Available for sale” financial assets are subsequently carried at fair value. Gains and losses arising from changes in the fair value of “Available for sale” financial assets are recognised directly in Other Comprehensive Income, until the financial asset is removed or impaired. At this time the cumulative gain or loss previously recognised in Other Comprehensive Income should be recognised in the Income Statement.

When the “Available for sale” assets are sold, unrealised gains or losses, previously recognised in Other Comprehensive Income, are transferred to the Income Statement item “Other net income (expense)” line “Gains / losses on disposal investment securities, equities available for sale”. In case of impairment losses, gains or losses previously recognised in Other Comprehensive Income, are transferred to the Income Statement item “Impairment losses” within the line “Impairment losses on investment securities, equities available for sale”.

The accounting policies affecting any dividend or interest earned on the financial assets “Available for sale” are disclosed later in the current Section, notes r and t.

For fair value measurement, refer to the disclosure in this paragraph under e1) Financial assets at fair value through profit or loss (FVTPL). For the rules on the impairment of financial assets pertaining to the category "Available for sale", refer to note u in the present Section.



### F) OFFSETTING FINANCIAL INSTRUMENTS

Financial assets and liabilities are offset and the net amount reported in the Balance Sheet only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

### G) DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGE ACCOUNTING

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into. The initial fair value generally corresponds to the initial cash consideration. They are subsequently remeasured at fair value through profit or loss.

The fair values of derivatives quoted in active markets are based on current bid prices. If the market for a financial derivative is not active, the IOR obtains fair values by market makers or establishes fair value by using valuation techniques, as well as considering prices utilised in recent transactions and prices of similar financial instruments. All derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. Derivative financial instruments may include the embedded derivatives in a hybrid financial instrument.

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

a) the economic risks and characteristics of the embedded derivative are not closely related to those of the host contract;
b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative;
c) the entire instrument is not measured at fair value with changes in fair value recognised in the Income Statement.

The Institute does not enter into Fair value hedge, Cash flow hedge or Net investment hedge transactions. On 31 December 2013, as well as on 31 December 2012, the Institute did not hold derivatives.

### H) GOLD, MEDALS AND PRECIOUS COINS

Gold, medals and precious coins are classified as current assets and stated at fair value since they are, held with the purpose of generating gains from price increases. Unrealised gains and losses are included in the Income Statement as Net trading income. Gold is stated at the PM fixing price on the London market on the last quotation day of the year. The different coins and medals are appraised on the basis of their weight and the quality of the gold and silver they contain.

### K) INVESTMENT IN SUBSIDIARIES

Investment in subsidiaries consists of the stake in the wholly-owned real estate company SGIR, located in Rome, Via della Conciliazione. The principal assets of this company are real estate properties and the Institute provides the entire financing to this company. Investment in subsidiaries is carried at cost less impairment. Real estate owned by the subsidiary is depreciated on a straight-line basis over its estimated useful life which management considers as between 30 and 50 years. Land is not depreciated.

### L) INVESTMENT PROPERTIES

Investment properties comprise of properties directly owned by the IOR and are buildings not owner-occupied but held to earn rental income or capital appreciation or both. Investment properties are initially measured at cost and subsequently at fair value with any change recognised in the Income Statement item “Other net income (expense)”. Improvements to buildings increase the carrying amounts.

### M) EQUIPMENT AND FURNISHINGS

All equipment is stated at historical cost, minus accumulated depreciation. Historical cost is generally based on the fair value of the sum paid in exchange for assets and includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset’s carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the IOR. All other repairs and maintenance are charged to the Income Statement during the financial period in which they are incurred. Equipment, furnishings and motor vehicles are amortised on straight-line basis over their expected useful lives (four years). The asset’s residual values and useful lives are reviewed, and adjusted if appropriate, on each balance sheet date. These assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset’s carrying amount is written down immediately to its recoverable amount if the asset’s carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset’s fair value less costs to sell and value in use. Gains and losses on disposals are determined as the difference between the sale proceeds and the carrying amount of the assets. They are recognised in the Income Statement, item “Other net income (expense)”.

## N) INTANGIBLE ASSETS

Intangible assets correspond to computer software licenses and to expenses related to their implementation. Acquired computer software licenses are recognised on the basis of the costs incurred to acquire and bring into use the specific software. These costs are amortised on a straight-line basis over their expected useful lives (four years). These assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. Costs associated with maintaining computer software programs are recognised as an expense when they are incurred.

## O) OTHER LIABILITIES

**Funds for Charitable Contributions**

The funds comprise the Fund at the disposal of the Commission of Cardinals, the Fund at the disposal of the Board of Superintendence, the Fund for Holy Masses and the Fund for Missionary Activities and they are included in the Balance sheet as "Other liabilities".

**Fund at the disposal of the Commission of Cardinalss**

The Fund at the disposal of the Commission of Cardinals is used to distribute charitable contributions approved by the Board to members of the Catholic Church. The Fund is financed by the distribution of the net profit of the year, following the decision of the Commission of Cardinals.

**Fund at the disposal of Board of Superintendence**

The Fund at the disposal of Board of Superintendence is used to distribute charitable contributions approved by the Board to members of the Catholic Church. The Fund is financed by the distribution of the net profit of the year, following the decision of the Commission of Cardinals.

**Fund for Missionary Activities**

The Fund for Missionary Activities is managed by the IOR Directorate and it is used to distribute contributions to congregations and institutions that operate missionary activities. The Fund is funded mainly by donations. Donations and distributions are recorded directly in the Fund account. Distributions to the beneficiaries are approved by a committee composed by the Prelate, the President, the General Manager and the Sales Manager.

**Fund for Holy Masses**

The Fund for Holy Masses is managed by the Directorate and is used to distribute contributions to priests for Holy Masses. The Fund is financed from donations. Donations and distributions are directly recorded in the Fund account. Distributions to the priests are approved by a committee composed by the Prelate, the President, the General Manager and the Sales Manager.

### P) POST-EMPLOYMENT BENEFITS

For the pensions of its employees, the IOR operates an unfunded defined benefit plan, which is financed by payments from employees and the IOR. The IOR's net liabilities in respect of defined benefit plans is calculated by estimating the amount of future benefit that employees will earn in return for their service in the current and prior periods; that benefit is discounted to determine its present value. The IOR determines the interest expense on the defined benefit liability for the period by applying the discount rate used to measure the same liability at the beginning of the annual period. The discount rate is the yield on the reporting date on high quality corporate bonds that have maturity dates approximating the terms of the IOR's liabilities and that are denominated in the currency in which the benefits are expected to be paid. The calculation is performed annually by a qualified actuary, who assessed the fairness of the liability, using the projected unit credit method. Remeasurements arising from the defined benefit plan comprise actuarial gains and losses. The IOR recognises them immediately in Other Comprehensive Income and all other expenses related to the defined benefit plan in Staff Expenses in the Income Statement. When the benefits of the plan are changed, the portion of the changed benefit related to past service by employees is recognised immediately in the Income Statement. On 1 January 2005, all IOR personnel also joined the general Vatican City State pension plan. This system is financed by contribution made by the Institute and employees. Contributions to the Vatican City State plan made by the IOR are recognised as employee benefit expense when they occur. Consequently, the IOR's defined benefit plan covers the entire amount to be paid by the Institute to employees for their service up to 31 December 2004. For the employees' services from 1 January 2005, only that portion not covered by the Vatican City State pension is the liability of the Institute taking into account the difference in the retirement age within the two pension systems. Other post-employment benefits correspond to indemnities paid to personnel when they leave the IOR. The amount due is based on years of service and salary paid in the last year of employment. These benefits are financed both from payments from employees and from the IOR contributions to the plan. The liability is measured with the actuarial methodology, assessing the liability towards employees at the present value of the estimated future cash outflows according to the projected unit credit method required by IAS 19. Remeasurements arising from the defined benefit plan comprise actuarial gains and losses. The IOR recognises them immediately in Other Comprehensive Income and all other expenses related to the defined benefit plan in Staff expenses within the Income Statement.

### Q) EQUITY

Equity Reserves are defined in the IOR statute and represent permanent capital not available for distribution. The Retained Earnings Reserve is a component of equity and consists of prior years' retained profits provisioned for the IOR's own financing needs and used for distributing profits even in less successful years. It is increased or decreased based upon net profit for the year less distribution. The Post-employment benefit actuarial gains (losses) Reserve represents the actuarial unrealised gain or loss related to the post-employment benefit plans.

### R) INTEREST INCOME AND EXPENSE

Interest income and expense are recognised in the Income Statement on an accruals basis. Interest income and expense for financial instruments classified as held for trading or designated at fair

value through profit or loss are recognised “pro rata temporis” based on the contractual interest rate. Interest Income and Expense for all remaining interest-bearing financial instruments, those classified as “Held to maturity” or classified as “Loans and receivables”, or classified as “Available for sale”, are recognised within “Interest Income” and “Interest Expense” in the Income Statement using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument (or where appropriate a shorter period) to the net carrying amount of the financial asset or financial liability on initial recognition. The calculation includes all transaction costs and all other premiums or discounts paid or received between parties to the contract that are an integral part of the effective interest rate.

## S) FEE AND COMMISSION INCOME AND EXPENSE

Fees and commissions are generally recognised when the service has been provided. Commissions arising from securities activities or other commissions (i.e. commissions for check issue or remittance or for payment orders) are recognised according to the contract relevant for the service provided, generally in the moment in which the service is provided. Commission from Asset management services are recognised on an accrual basis over the period that the service is provided.

## T) DIVIDENDS

Dividends on trading securities and available for sale equity instruments are recognised in the Dividend income when the entity’s right to receive payment is established.

## U) IMPAIRMENT OF FINANCIAL ASSETS

**u1) Assets carried at amortised cost – Loans and advances to customers and securities loans and receivables**

On each balance sheet date, the IOR assesses whether there is objective evidence that a financial asset is impaired. A financial asset is impaired and impairment losses are incurred if:

- there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset, or
- that loss event has an impact on the estimated future cash flows of the financial asset.

If this relates to credits valued at amortised cost, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows discounted at the financial asset’s original effective interest rate. The carrying amount of the asset is reduced through the use of a provision account and the extent of the loss is recognised in the Income Statement item “Impairment losses”. Loans which are not individually impaired are impaired on a portfolio

basis based on the loss experience. If, in a subsequent period, the extent of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the Income Statement as "Other net income (expense)". When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the extent of the loss has been determined. Subsequent recoveries of amounts previously written off are recognised in the Income Statement as "Other net income (expense)".

**u2) Assets carried at amortised cost – Held to maturity financial assets**
On each balance sheet date, the IOR assesses whether there is objective evidence that a financial asset is impaired. A financial asset is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a "loss event") and that loss event has an impact on the estimated future cash flows of the financial asset that can be reliably estimated. For Held to maturity financial assets, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows and it is recognised in the Income Statement, item "Impairment losses". If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is directly reversed. However, the reversal cannot result in a carrying amount of the financial asset that exceeds what the amortised cost would have been had no impairment been recognised. The amount of the reversal is recognised in the Income Statement.

**u3) Assets classified as available for sale**
On each balance sheet date, the IOR assesses whether there is objective evidence that a financial asset is impaired. A significant or prolonged decline in the fair value of the financial asset below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available for sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in Income Statement – is removed from equity and recognised in the Income Statement item "Impairment losses". Impairment losses recognised in the Income Statement on equity instruments are not reversed through the Income Statement, if, in a subsequent period, the amount of the impairment loss decreases.

For debt instruments, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the Income Statement. The impairment policy adopted by the IOR is that all shares classified as available for sale must be impaired when their market prices are below their carrying prices and the price decline is more than 20 %, or when the decline to below the acquistion cost has persisted for more than 36 months.

### V) ASSETS HELD UNDER CUSTODY AGREEMENTS

These off balance sheet assets include mainly customer-owned securities kept by customers at the IOR for custodial purposes. The customers make all investment decisions and the IOR has no discretionary power to manage these assets. Securities gold and precious metals are stated at market values.

### W) ASSETS HELD UNDER PORTFOLIO MANAGEMENT AGREEMENTS

These off balance sheet assets include mainly customer-owned securities lodged by customers at the IOR for management purposes. Investment decisions are taken by the IOR on the basis of a portfolio management agreement signed by the customers. Securities are stated at market values.

SECTION III



# Critical accounting estimates and judgments

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

Such circumstances and related judgments may form part of the evaluation process used for financial instruments. The Directorate makes critical judgments when deciding the category under which to classify financial assets, defining whether a market is active or not, whether it is liquid or illiquid, which market inputs and parameters are to be used, when they must be reviewed, in which circumstances internal parameters are more reliable than market-based ones, and so on.

Retirement benefits and other post-employment liabilities are also based on critical judgements because estimates are made about the likelihood of future events and the actual results could differ from those estimates.

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

Key assumptions in the 2014 Financial Statements are represented by the judgement related to the assessment of illiquid debt securities in the trading portfolio and of some of external investment funds included within the portfolio of trading securities, as disclosed in Section IV note 27 "Fair value information". Illiquid securities are not quoted in active markets and their fair value is not readily available in the market. The securities subject to key sources of estimation uncertainties (Level 3 of fair value hierarchy) amounted to EUR 35.9 m on 31 December 2014 (2013: EUR 42.4 m). These were composed exclusively of externally managed investment funds.

The IOR has also been working to review and confirm its tax position and that of its customers towards countries with which they have investment relationships. This work has identified probable contingencies which relate to prior years as a result of different interpretations regarding the legal nature of the Institute and the consequent related tax treatments. At this stage, no reliable estimate can be made. As a consequence, under the provision of IAS 37 par. 26, no specific provision has been accounted for in the 2014 Financial Statements. However, the IOR remains fully committed to addressing any incorrect treatment with the relevant tax authorities having the capacity to meet any payments that may arise from the above review.

SECTION IV

# Explanatory notes to the financial statements



## ASSETS

### 1. CASH AND BANK DEPOSITS

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Cash | 16,351 | 38,784 |
| Due from banks on demand | 283,281 | 274,576 |
| Term deposits due from banks (< 90 days) | 181,000 | 379,621 |
| Cash and cash equivalents | 480,632 | 692,981 |
| Term deposits due from central banks (> 90 days) | 35,000 | – |
| Term deposits due from other banks (> 90 days) | 50,000 | – |
| Accruals | 1,726 | 9 |
| Other deposits | – | 23,000 |
| | **567,358** | **715,990** |

The item "Cash and cash equivalents" comprises cash, due from banks on demand and other bank deposits with less than 90 days maturity from the date of acquisition. The same item is used for the purposes of the cash flow statement. During 2014, a sum of EUR 23 m, deposited at an Italian bank and classified as Other deposits in 2013, became fully available. In 2014, the Institute earned an average interest of 0.66 % (2013: 0.71 %) on its bank deposits.

### 2. TRADING SECURITIES

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| **DEBT SECURITIES AND BONDS** | | |
| Government | 660,285 | 595,225 |
| Other government entities, agencies, banks and other | 957,237 | 827,505 |
| | 1,617,522 | 1,422,730 |
| Accruals | 10,348 | 11,296 |
| | 1,627,870 | 1,434,026 |
| Listed equity securities | 13,005 | 64,173 |
| Externally managed investment funds | 77,261 | 250,702 |
| | **1,718,136** | **1,748,901** |

At the closing date of the financial statements, the item Trading securities was little changed from 31 December 2013 (– 1.8 %). As shown in the table, the main difference was a change in the strategy adopted by the Institute. With the aim of de-risking the proprietary portfolio, the Directorate decided to increase investment in bonds, and correspondingly reduce investment in equities and external investment funds (EUR 90.3 m in 2014, versus EUR 314.9 m in 2013). Both the bond portfolio, which posted realised and unrealised profits of EUR 25.4 m, and the external investment funds, which posted realised profits of EUR 10.3 m, performed well. For further details, please see Note 20 of the current

Section. In fact, the bond market performed very well after the reduction of interest rates during the year. On the external investment funds side, the Institute sold an external investment fund, resulting in realised profits of EUR 9.7 m.



## 3. GOLD, MEDALS AND PRECIOUS COINS

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Gold | 22,762 | 20,010 |
| Medals and precious coins | 10,446 | 9,857 |
| **Total** | **33,208** | **29,867** |

During 2014, the value of gold carried on the balance sheet increased by 11 %. This was mainly due to the appreciation of USD, which is the base currency for the gold owned by the IOR (around EUR 2.6 m) as well as new purchases (around EUR 0.7 m). The main depository for gold is the US Federal Reserve, while medals and precious coins are kept in the IOR vaults. Gold is carried at market value.

## 4. DERIVATIVE FINANCIAL INSTRUMENTS

As of 2014 year-end, as well as of 2013 year-end, the IOR did not hold any derivative financial instruments.

## 5. LOANS AND ADVANCES TO CUSTOMERS

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Loans | 7,669 | 9,470 |
| Credit lines utilised | 26,249 | 27,487 |
| Overdrafts | 880 | 1,914 |
| Long term advances to subsidiary | 3,893 | 4,265 |
| Provision for specific impairment losses | (10,237) | (8,762) |
| Provision for impairment losses for interest-free loans | (4,782) | (3,199) |
| Allowance for portfolio impairment losses | (1,264) | (1,713) |
| | **22,408** | **29,462** |

| *Movement in the specific impairment losses is as follows:* | | |
|---|---|---|
| Balance at 1 January | 8,762 | 6,745 |
| Loans written off during the year as uncollectible | – | – |
| Specific impairment losses on loans and advances | 2,183 | 2,042 |
| Reversal of impairment losses for amounts recovered | (708) | (25) |
| **Balance at 31 December** | **10,237** | **8,762** |

The item “Loans and advances to customers” recorded a decrease of 23.9 %. Gross credits fell due to fewer loans and credit lines being granted during the year, and impairment losses increased due to new provisions. The provision for specific impairment losses rose 16.8 % due to new provisions concerning credit positions considered totally or partially irrecoverable. As an adjustment to the item, an impairment amounting to EUR 4.8 m is listed, related to a zero-interest loan granted in 2013 in accordance with the mission of the Institute (of which EUR 1.6 m was provisioned for in 2014 and EUR 3.2 m in 2013).

## 6. LOANS AND RECEIVABLES SECURITIES

| | 2014 | 2013 |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Debt securities and bonds | 183,169 | 244,772 |
| Accruals | 4,508 | 6,098 |
| | **187,677** | **250,870** |

*Movement in the item may be summarised as follows:*

| | 2014 | 2013 |
|---|---|---|
| Balance at 1 January | 250,870 | 252,252 |
| Additions | – | – |
| Redemption at maturity | (66,288) | – |
| Amortisation | 3 | 2 |
| Reversal accruals previous year | (6,098) | (5,831) |
| Accruals | 4,508 | 6,098 |
| FX effects | 4,682 | (1,651) |
| **Balance at 31 December** | **187,677** | **250,870** |

The securities included under this item on 31 December 2014 and on 31 December 2013 are bonds deriving from private placements. The fair value of this category of securities, net of accruals, was EUR 182.2 m, with a negative difference of EUR 1 m compared to the carrying value. For most of the bonds classified as Loans and Receivables, the fair value is lower than the carrying value, but the IOR Directorate considers these investments fully recoverable considering the high standing of the issuers.

## 7. INVESTMENT SECURITIES, EQUITIES AVAILABLE FOR SALE

| | 2014 | 2013 |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| **LISTED EQUITY SECURITIES** | 10,382 | 13,922 |
| **UNLISTED EQUITY SECURITIES** | 8 | 8 |
| | **10,390** | **13,930** |

*Movement in the item may be summarised as follows:*

| | 2014 | 2013 |
|---|---|---|
| Balance at 1 January | 13,930 | 9,619 |
| Additions | 6,321 | – |
| Disposals | (2,432) | (1,214) |
| Impairment | (1,985) | (198) |
| Reclassification adjustments relating to investment securities available for sale disposed in the year (note 22) | (76) | 355 |
| Reversal of Fair Value Loss on investment securities at impairment into Income Statement | – | – |
| Reversal to reserve of fair value gain (loss) on available for sale investment securities recorded in the prior years | (5,368) | – |
| Gains (losses) from changes in fair value | – | 5,368 |
| **Balance at 31 December** | **10,390** | **13,930** |

In 2014, the Institute purchased EUR 6.3 m in new shares, following the capital increase approved by the issuer of an “Available for Sale” security. In addition, in 2014, the Institute sold some “Available for Sale” shares, generating a loss of EUR 76,000, which is recorded in the Income Statement under

"Other net income (expense)" (note 22). In 2014, another investment was impaired by EUR 2 m, which is recognised in the Income Statement item "Impairment losses" (note 23), due to the further decline in its fair value to below the historical cost.



## 8. HELD TO MATURITY SECURITIES

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Debt securities and bonds | 637,865 | 568,217 |
| Accruals | 7,189 | 6,599 |
| | **645,054** | **574,816** |

*Movement in the item may be summarised as follows:*

| | *2014* | *2013* |
|---|---|---|
| Balance at 1 January | 574,816 | 626,764 |
| Additions | 174,061 | 139,337 |
| Early mandatory redemption | (36,796) | – |
| Redemption at maturity | (70,000) | (193,183) |
| Amortisation | (2,366) | 3,809 |
| Reversal accruals previous year | (6,599) | (6,754) |
| Accruals | 7,189 | 6,599 |
| FX Effect | 4,749 | (1,756) |
| **Balance at 31 December** | **645,054** | **574,816** |

The fair value of this securities category, net of accruals, was EUR 680.9 m. This item mainly comprises government bonds issued by European countries and bonds issued by supranational financial entities.

## 9. INVESTMENT IN SUBSIDIARIES

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Stakes in real estate companies | 15,835 | 15,835 |
| | **15,835** | **15,835** |

The value of the stake in the real estate company SGIR is unchanged. SGIR is 100 % owned by the IOR. As of 31 December 2014, its equity amounted to EUR 22 m, including EUR 12.4 m for SGIR's Fiscal Revaluation Reserve. SGIR has its registered office in Italy.

## 10. INVESTMENT PROPERTIES

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Directly owned properties | 2,181 | 2,126 |
| | **2,181** | **2,126** |

| *Movement in the item may be summarised as follows:* | | |
|---|---|---|
| Balance at 1 January | 2,126 | 1,914 |
| Additions | – | – |
| Sale of real estate investment properties | – | – |
| Improvement to buildings | 73 | – |
| Gains (losses) from changes in fair value of Investment properties | (18) | 212 |
| **Balance at 31 December** | **2,181** | **2,126** |

The item totalled EUR 2.2 m. The slight increase from 31 December 2013 was due to the renovation of a property, which increased in value by EUR 73,000. For other properties, the Institute received a report from a qualified independent expert, concerning the year 2014, which confirmed the value registered in 2013, except in the case of one property which lost EUR 18,000 in value. In 2014, the properties did not produce any income since there were no leasing agreements in place. One property is subject to a life-long grant of use.

## 11.a EQUIPMENT AND FURNISHINGS

| | *Furniture & fittings* | *Office equipment* | *Motor vehicles* | *Total* |
|---|---|---|---|---|
| | *EUR 000* | *EUR 000* | *EUR 000* | *EUR 000* |
| **BALANCE AT 31 DECEMBER 2013** | | | | |
| Original cost | 2,628 | 4,295 | 32 | 6,955 |
| Accumulated depreciation | (2,585) | (4,159) | (9) | (6,753) |
| **Closing net book amount** | **43** | **136** | **23** | **202** |
| **YEAR ENDED 31 DECEMBER 2014** | | | | |
| Opening net book amount | 43 | 136 | 23 | 202 |
| Additions | – | 15 | – | 15 |
| Disposals | – | – | – | – |
| Depreciations | (16) | (73) | (5) | (94) |
| **Closing net book amount** | **27** | **78** | **18** | **123** |
| **Disposal of assets completely depreciated** | – | – | – | – |
| **Disposal of assets under depreciation** | – | – | – | – |
| **BALANCE AT 31 DECEMBER 2014** | | | | |
| Original cost | 2,628 | 4,310 | 32 | 6,970 |
| Accumulated depreciation | (2,601) | (4,232) | (14) | (6,847) |
| **Closing net book amount** | **27** | **78** | **18** | **123** |

## 11.b INTANGIBLE ASSETS

| | *Computer software & licenses* |
|---|---|
| | *EUR 000* |
| **BALANCE AT 31 DECEMBER 2013** | |
| Original cost | 5,440 |
| Accumulated depreciation | (4,341) |
| **Closing net book amount** | **1,099** |
| **YEAR ENDED 31 DECEMBER 2014** | |
| Opening net book amount | **1,099** |
| Additions | 235 |
| Disposals | – |
| Depreciations | (501) |
| **Closing net book amount** | **833** |
| **Disposal of intangible assets completely depreciated** | – |
| **BALANCE AT 31 DECEMBER 2014** | |
| Original cost | 5,675 |
| Accumulated depreciation | (4,842) |
| **Closing net book amount** | **833** |

The IOR does not have internally generated intangible assets.

## 12. OTHER ASSETS

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Sundry debtors | 7,072 | 7,394 |
| Prepayments | 500 | 502 |
| Securities sold not settled | – | 23 |
| **Total** | **7,572** | **7,919** |

The item Other Assets includes EUR 6.1 m for Commission from Asset Management services not yet received at the closing date of the financial statements. These commissions, pertaining to the second half of 2014, were collected in the first days of 2015. Furthermore, the item included EUR 692,000 deposited as guarantees for VISA transactions and EUR 197,000 in advances for VISA transactions.

## LIABILITIES

### 13. DUE TO BANKS

The item Due to Banks includes a small overdraft of EUR 16,000 (2013: EUR 600).

### 14. DUE TO DEPOSITORS

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Deposits on demand | 2,200,638 | 2,159,747 |
| Term deposits | 158,476 | 377,502 |
| Accruals | 2,749 | 7,029 |
| **Total** | **2,361,863** | **2,544,278** |

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

These are composed of:

| **DEPOSITS ON DEMAND AND TERM DEPOSITS RELATED TO ASSET MANAGEMENT ACCOUNTS** | | |
|---|---|---|
| Deposits on demand | 296,354 | 506,470 |
| Term deposits | – | 166,635 |
| | **296,354** | **673,105** |

The item Due to depositors recorded a decrease from 2013, mainly due to the reduction of Deposits on demand and of Term deposits related to Asset Management accounts for which the IOR is the depository institution. The main reason was the IOR asset manager's decision to invest directly in securities rather than in cash and term deposits, in order to optimise returns. The item Due to depositors includes a deposit at the Commission of Cardinals disposal to support works of religion. At the closing date of the financial statements, this amounted to EUR 10.8 m, in addition to the fund detailed in the item Other liabilities (note 15).

### 15. OTHER LIABILITIES

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Sundry creditors | 24,965 | 33,224 |
| Funds for charitable contributions | 3,585 | 3,293 |
| Liabilities for guarantees issued and commitments towards third parties | 1,405 | – |
| Securities purchased not settled | – | 3 |
| **Total** | **29,955** | **36,520** |

| *Sundry Creditors comprise:* | | |
|---|---|---|
| Inheritances to be settled | 16,932 | 24,435 |
| Invoices to be received | 5,227 | 5,074 |
| Outstanding cheques | 1,564 | 1,849 |
| Remunerations to be paid | 898 | 1,228 |
| Unsettled amounts | 146 | 605 |
| Other | 198 | 33 |
| | **24,965** | **33,224** |

The item "Inheritances to be settled" consists of legacy outstanding balances owned by deceased clients pending the outcome of inheritance. The EUR 1.4 m listed above under "Other liabilities" are due to guarantees on two asset management positions and commitments to third parties amounting to EUR 4 m (see note 24). The breakdown of Funds for charitable contributions is as follows:

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Fund at the disposal of the Commission of Cardinals | 425 | 425 |
| Fund at the disposal of Board of Superintendence | – | – |
| Fund for Missionary Activities | 189 | 139 |
| Fund for Holy Masses | 2,971 | 2,729 |
| | **3,585** | **3,293** |

The movement of the Funds for charitable contributions is summarised as follows:

| **FUND AT THE DISPOSAL OF THE COMMISSION OF CARDINALS** | *2014* | *2013* |
|---|---|---|
| Balance at 1 January | 425 | 425 |
| Appropriations: | | |
| Donations received | – | – |
| Transfer from earnings available for distribution | – | – |
| Distributions: | | |
| Charitable distributions | – | – |
| **Balance at 31 December** | **425** | **425** |

| **FUND AT THE DISPOSAL OF BOARD OF SUPERINTENDENCE** | | |
|---|---|---|
| Balance at 1 January | – | – |
| Appropriations: | | |
| Donations received | – | – |
| Transfer from earnings available for distribution | – | – |
| Distributions: | | |
| Charitable distributions | – | – |
| **Balance at 31 December** | **–** | **–** |

| **FUND FOR MISSIONARY ACTIVITIES** | | |
|---|---|---|
| Balance at 1 January | 139 | 129 |
| Donations received | 67 | 10 |
| Distributions for Missionary Activities | (17) | – |
| **Balance at 31 December** | **189** | **139** |

| **FUND FOR HOLY MASSES** | | |
|---|---|---|
| Balance at 1 January | 2,729 | 2,178 |
| Donations received | 277 | 610 |
| Distributions for Holy Masses | (35) | (59) |
| **Balance at 31 December** | **2,971** | **2,729** |

Distributions of funds to beneficiaries are subject to strict internal policies as per an agreed governance.

## 16. POST-EMPLOYMENT BENEFIT PLANS

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| *Amounts recognised in the Balance Sheet:* | | |
| Benefit plan for pensions | 117,396 | 84,681 |
| Other post employment benefit plan | 6,551 | 5,490 |
| **Total** | **123,947** | **90,171** |

Movement in the defined benefit plan liability for pensions recognised in the Balance Sheet is summarised as follows:

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Balance at 1 January | 84,681 | 81,526 |
| Current costs (note 21bis) | 3,003 | 3,196 |
| Contribution by individuals | 81 | 218 |
| Tranfers from other post employment benefit | – | 120 |
| Pensions paid during the year | (3,051) | (2,842) |
| Transfers out | (37) | – |
| Actuarial (gain) loss of the year | 32,719 | 2,463 |
| **Balance at 31 December** | **117,396** | **84,681** |
| *Amounts recognised in the Income Statement:* | | |
| Current service cost | 367 | 412 |
| Interest cost | 2,636 | 2,743 |
| New employments cost | – | 41 |
| **Total, included in staff expenses (note 21 bis)** | **3,003** | **3,196** |

The actuarial valuation of the defined benefit plan liability for pensions was performed taking into account the following assumptions:

| | | |
|---|---|---|
| Annual inflation rate | 2.00 % | 2.00 % |
| Annual discount rate | 1.58 % | 3.15 % |
| Annual rate for revaluation of pension | 2.00 % | 2.00 % |
| Annual rate of real increase salary | 2.50 % | 2.50 % |

The Current Service Cost is the actuarial present value of benefits attributed by the pension formula to employee service performed in the period.

The Interest Cost is the increase in the present value of the obligation as a result of moving one period closer to settlement and is proportional to the actuarial rate used in the assessment and to the previous year's liabilities.

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

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

The Actuarial gain / loss is recognised directly to Equity in a specific reserve named "Post-employment benefit actuarial gain (loss) reserve" and the results are recorded in Other Comprehensive Income. A total of 110 employees are active and contribute to the Pension plan. A total of 72 people are in retirement and benefit from the plan (2013: 110 – 70). The other liability is the post-employment benefit plan.

Movement in the other post employment benefit recognised in the Balance Sheet is summarised as follows:

| | 2014 | 2013 |
|---|---|---|
| | EUR 000 | EUR 000 |
| Balance at 1 January | 5,490 | 5,369 |
| Current costs (note 21bis) | 429 | 445 |
| Contribution by individuals | 72 | 107 |
| Tranfers to benefit plan for pensions | – | (120) |
| Advances | (155) | (100) |
| Advances restitution | 49 | 88 |
| Consideration paid during the year | (634) | (581) |
| Actuarial (gain) loss of the year | 1,300 | 282 |
| **Balance at 31 December** | **6,551** | **5,490** |

The actuarial assumptions used for the valuation of the other post-employment benefits are the same as those used for the Benefit Plan Liability for pensions. For both post-employment benefits, in 2014, the Institute recognised an actuarial loss of EUR 34 m (2013: EUR 2.7 m) in Other Comprehensive Income. Consequently, the post-employment actuarial gain (loss) reserve showed a negative result of EUR 41.6 m (2013: EUR – 7.6 m); the significant increase compared to the previous year is due to the reduction of the discount rate, which went from 3.15 % in 2013 to 1.58 % in 2014.

## INCOME STATEMENT

### 17. NET INTEREST RESULT

| | 2014 | 2013 |
|---|---|---|
| | EUR 000 | EUR 000 |
| **INTEREST INCOME** | | |
| Bank deposits | 4,179 | 5,079 |
| Trading securities | 30,049 | 39,384 |
| Loans and receivables securities | 9,263 | 10,066 |
| Held to maturity securities | 16,853 | 20,907 |
| Loans and advances to customers | 744 | 920 |
| | **61,088** | **76,356** |
| **INTEREST EXPENSE** | | |
| Customers deposits | 10,414 | 22,530 |
| Other | 14 | 14 |
| | **10,428** | **22,544** |

Interest income on Loans and Receivables securities and on investment securities Held to Maturity include the premium or the discount amortisation. In 2014, the Institute recorded a general decrease in all items related to Interest margin, both income and expense, due to the reduction in interest rates by the European Central Bank. The main impact was on the item interest expense on customer deposits (– 54 %).

## 18. NET FEE AND COMMISSION RESULT

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| **FEE AND COMMISSION INCOME** | | |
| Commission from Asset management services | 12,647 | 13,309 |
| Commissions from Custody services | 2,099 | 2,754 |
| Other fees received | 1,920 | 1,528 |
| | **16,666** | **17,591** |

| | *2014* | *2013* |
|---|---|---|
| **FEE AND COMMISSION EXPENSE** | | |
| Fees paid for brokerage | 588 | 1,556 |
| Fees paid for securities custody | 902 | 913 |
| General fees paid to banks | 662 | 836 |
| Other fees paid | 152 | 176 |
| | **2,304** | **3,481** |

The decrease of Fee and Commission income is mainly due to the reduction of Commissions from Asset management services (– 5.3 %) and of Commission received for custody and administration (– 23.8 %), due to the decrease of assets under custody agreements. The decline in Fee and Commission expense is due mainly to the decline of Fees paid for brokerage (– 62.2 %), which in turn was due to fewer transactions on equities. Meanwhile, Fees paid to banks also fell by 20.8 % due to the rationalisation of the IOR's external banking relationships.

## 19. DIVIDEND INCOME

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Trading securities | 2,527 | 3,298 |
| Investment securities available for sale | 254 | 498 |
| | **2,781** | **3,796** |

In 2014, the dividend income from trading securities was EUR 2.5 m (2013: EUR 3.3 m), a decline of 23.4 %. In 2014, the Institute received dividends of EUR 254,000 relating to an investment security (2013: EUR 498,000).

## 20. NET TRADING RESULT

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| Foreign exchange | 1,581 | 711 |
| Debt securities and bonds | 25,450 | (760) |
| Equity securities | 1,314 | 12,868 |
| External investment funds | 7,764 | (17,890) |
| Gold, medals and precious coins | 608 | (11,474) |
| Derivative financial instruments | – | – |
| | **36,717** | **(16,545)** |

The two tables below show the breakdown of the item “Net trading result” distinguishing between realised result and unrealised result.

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| | *Realised gain / loss* | *Realised gain / loss* |
| Foreign exchange | 1,551 | 608 |
| Debt securities and bonds | 14,767 | 5,285 |
| Equity securities | 742 | 12,063 |
| External investment funds | 10,294 | 385 |
| Gold, medals and precious coins | 27 | (48) |
| Derivative financial instruments | – | – |
| | **27,381** | **18,293** |

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| | *Unrealised gain / loss* | *Unrealised gain / loss* |
| Foreign exchange | 30 | 103 |
| Debt securities and bonds | 10,683 | (6,045) |
| Equity securities | 572 | 805 |
| External investment funds | (2,530) | (18,275) |
| Gold, medals and precious coins | 581 | (11,426) |
| Derivative financial instruments | – | – |
| | **9,336** | **(34,838)** |
| **Total Net Trading result** | **36,717** | **(16,545)** |

The following summarises the net trading results in 2014, compared to 2013.
The increase is due to the growth of:

- realised result from debt securities and bonds (in 2014 a gain of EUR 14.8 m from a gain of EUR 5.3 m in 2013);
- realised result from external investment fund (in 2014 a gain of EUR 10.3 m from a gain of EUR 400,000 in 2013);
- unrealised result from debt securities and bonds (in 2014 a gain of EUR 10.7 m from a loss of EUR 6 m in 2013);
- unrealised result from external investment funds (in 2014 a loss of EUR 2.5 m from a loss of EUR 18.3 m in 2013);
- the price of gold that lead to a gain of EUR 600,000 from a loss of EUR 11.5 m.

## 21. OPERATING EXPENSES

| | 2014<br>EUR 000 | 2013<br>EUR 000 |
|---|---|---|
| Staff expenses (note 21 bis) | 10,793 | 11,995 |
| Depreciation of equipment and furnishings (note 11a) | 94 | 168 |
| Depreciation of intangible assets (note 11b) | 501 | 491 |
| Other operating expenses | 17,492 | 19,533 |
| | **28,880** | **32,187** |

In 2014, operating expenses fell by 10.3 %, mainly due to the decrease of the item "Other operating expenses", which was EUR 17.5 m in 2014 (2013: EUR 19.5 m or – 10.3 %), and of the item "Staff expenses" which was EUR 10.8 m in 2014, compared to EUR 12 m in 2013 (– 10 %). The details of the item "Staff expenses" are given in the next note (note 21 bis), while the item's depreciation of tangible and intangible assets are detailed in notes 11a and 11b. A further explanation is required for the item "Other operating expenses". The 10.3 % decline was due to the termination of some projects, such as those related to meeting international anti-money laundering and compliance requirements.
The item "Other operating expenses" also includes a provision of EUR 1 m payable to the owner of the building in which the IOR conducts business.

## 21 bis. STAFF EXPENSES

| | 2014<br>EUR 000 | 2013<br>EUR 000 |
|---|---|---|
| Wages and other indemnities | 6,684 | 7,657 |
| Pension costs: contributions to the vatican pension plan | 677 | 697 |
| Pension costs: defined benefit plan (note 16) | 3,003 | 3,196 |
| Other post employment benefits (note 16) | 429 | 445 |
| | **10,793** | **11,995** |

Staff expenses fell 10 % from the previous year, because in 2013 this item was affected by indemnities related to the termination of the contracts with the Directorate in charge until 30 June 2013.
The IOR contributed a total of EUR 3.7 m (2013: EUR 3.9 m) to the Vatican City State pension fund, as well as the IOR's own pension fund, since the Vatican City State pension plan was only joined in 2005 (note 16).

## 22. OTHER NET INCOME (EXPENSE)

| | 2014<br>EUR 000 | 2013<br>EUR 000 |
|---|---|---|
| Recovery of amounts for doubtful loans previously impaired (note 5) | 708 | 25 |
| Reversal exceeding allowance for portfolio impairment losses (note 5) | 449 | – |
| Gain (loss) on disposal investment securities, equities available for sale (note 7) | (76) | 355 |
| Gain (loss) from changes in fair value of investment properties (note 10) | (18) | 212 |
| Liberality | – | (15,128) |
| Other | (213) | 140 |
| | **850** | **(14,396)** |

In 2014, the item recorded a positive balance mainly due to the recovery of amounts for doubtful loans previously impaired. In contrast, in 2013, the item was negative because it included the donation of securities to third parties, in accordance with the mission of the Institute.

## 23. IMPAIRMENT LOSSES

| | 2014 | 2013 |
|---|---|---|
| | EUR 000 | EUR 000 |
| Specific impairment losses on loans and advances (note 5) | 2,184 | 2,042 |
| Impairment for interest-free loans (note 5) | 1,583 | 3,198 |
| Allowance for portfolio losses on loans and advances (note 5) | – | 287 |
| Impairment losses on investment securities, equities available for sale (note 7) | 1,985 | 198 |
| Impairment for guarantees issued and for commitments towards third parties (note 15) | 1,405 | – |
| | **7,157** | **5,725** |

In 2014, the specific impairment losses on loans and advances to customers were little changed from 2013 (EUR 2.2 m in 2014, compared to EUR 2 m in 2013). The impact on the Income Statement of a zero-interest loan, provided in accordance with the IOR's mission, was EUR 1.6 m in 2014, down from EUR 3.2 m in 2013. In 2014, there was a significant increase in impairment losses on investment equities available for sale. These amounted to EUR 2 m in 2014 (2013: EUR 198,000). In addition, in 2014, this item contained a new impairment of EUR 1.4 m due to guarantees issued in favour of customers as well as commitments towards third parties.

## 24. CONTINGENT LIABILITIES AND COMMITMENTS

| | 2014 | 2013 |
|---|---|---|
| | EUR 000 | EUR 000 |
| Guarantees issued in favour of third parties | 53 | 79 |
| Commitments towards third parties | 4,000 | 4,000 |
| | **4,053** | **4,079** |

At the closing date of the financial statements, the Institute has a commitment of EUR 4 m issued in favour of third parties. The IOR issued two guarantees covered by assets held in custody. No new guarantees were issued in 2014. The guarantees were initially recognised at their nominal value, which is their fair value. In subsequent periods, the guarantees are reported at the amount determined in accordance with IAS 37 “Provisions, Contingent Liabilities and Contingent Assets”.

## 25. THIRD PARTIES' VALUES

| | 2014 EUR 000 | | |
|---|---|---|---|
| | *On Balance Sheet* | *Off Balance Sheet* | *Total* |
| Customers Deposits (on demand and term deposits) | 2,065,509 | – | 2,065,509 |
| Assets under Management agreements | 296,354 | 2,927,022 | 3,223,376 |
| Assets under Custody agreements | – | 673,209 | 673,209 |
| **Total** | **2,361,863** | **3,600,231** | **5,962,094** |

| | 2013 EUR 000 | | |
|---|---|---|---|
| | *On Balance Sheet* | *Off Balance Sheet* | *Total* |
| Customers Deposits (on demand and term deposits) | 1,871,173 | – | 1,871,173 |
| Assets under Management agreements | 673,105 | 2,645,328 | 3,318,433 |
| Assets under Custody agreements | – | 758,842 | 758,842 |
| **Total** | **2,544,278** | **3,404,170** | **5,948,448** |

The Assets under Management agreements are evaluated according to the mark to market method. They include the total value of portfolios, and consequently also the liquidity for settlements and term deposits. Accruals are also included, both on securities and on liquidity and term deposits. The IOR is the depository for the liquidity for settlements and for term deposits, amounting to EUR 296.4 m (2013: EUR 673.1 m), as disclosed in note 14. Assets under custody agreements are also based on current bid prices, according to the mark to market method. They also include accruals on interests to be received on debt securities.

## 26. RELATED PARTY TRANSACTIONS

IAS 24 "Related party Disclosures" requires the disclosure of the nature and amounts of related party transactions and outstanding balances in the financial statements of the reporting entity. In the IOR's case, related parties comprise key management personnel (Directorate and Board of Superintendence) and the Commission of Cardinals. The transactions with these related parties relate to ordinary emoluments and salaries. The expenses for compensation to related parties were EUR 630,000 in 2014 (2013: EUR 1.6 m), of which EUR 130,000 were accounted for but not yet paid out by 31 December 2014.

Specifically, these expenses refer to:

- EUR 132,000 for the President of the Board of Superintendence, in office until 8 July.
- EUR 93,000 for the President of the Board of Superintendence, in office from 9 July.
- EUR 175,000 for the Directorate.
- EUR 130,000 for the Board of Superintendence, in office until 8 July, of which EUR 30,000 has not yet been paid out.
- EUR 100,000 for the Board of Superintendence, in office from 9 July, which has also not yet been paid.

They are recognised in the Income Statement as Operating Expenses.

At the closing date of these Financial Statements, EUR 694,000 in benefits for mutual termination agreements had also not yet been paid. These were accounted for in 2013 following the departure of the two members of the Directorate in charge up to 30 June 2013. At the closing date of these Financial Statements, the balance of deposits of the members of the Commission of Cardinals was EUR 2.3 m. The key management personnel had deposits for EUR 28,000. The Institute has a long-term zero-interest loan to its subsidiary SGIR, amounting to EUR 3.8 m. The IOR also signed an agreement for administrative services related to real estate properties, and during 2014, it paid EUR 12,200 to SGIR.

## 27. FAIR VALUE INFORMATION

On 1 January 2013, the Institute became an early adopter of the IFRS 13 "Fair Value Measurement" standard, which consolidates within a single accounting standard all rules relating to the determination of the fair value previously included in different accounting standards. The standard keeps the concept of fair value essentially unchanged, and clarifies how it is to be determined by providing a set of practical, complete and shared instructions for its use. It also expands the scope of information within the financial statements.

### Fair Value Hierarchy

The fair value hierarchy provides three levels according to the degree of observability of the inputs, the valuation techniques adopted and parameters used for measurement.

#### LEVEL 1

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

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

- promptly and regularly available on stock exchanges, information providers or intermediaries;
- significant, meaning that it represents effective market transactions regularly occurring in normal transactions.

To be considered Level 1, the price should be unadjusted. It should not be adjusted through a valuation adjustment. If it is adjusted, the relevant level is Level 2 or Level 3.

#### LEVEL 2

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

The parameters of Level 2 are as follows:

- prices quoted in active markets for similar assets or liabilities;
- less-active markets for the same or identical assets and liabilities;

- market observable inputs other than the quoted price for the asset or liability (interest rates, yield curve, credit spreads, volatility);
- parameters that derive mainly (or are corroborated by correlation or other techniques) by observable market data (market-corroborated inputs).

An input is observable when it reflects the assumptions that market participants would use in pricing an asset or liability based on market data provided by sources independent from the reporting entity. Valuation techniques used for fair value, that should be used only if the market price is not available or it is not significant, must meet three conditions. They must:

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

Valuation techniques used for fair value measurement should be periodically assessed using inputs observable in the markets to ensure that outputs reflect actual data and comparative market prices and to identify any weaknesses. If the fair value measurement utilises observables that require a significant adjustment based on unobservable inputs, the valuation has to be considered in Level 3.

### LEVEL 3

Included in Level 3 are financial instruments evaluated using inputs not based on observable market data (unobservable inputs). To be included in Level 3, at least one of the inputs must be unobservable in the market. Specifically Level 3 should be used when inputs are not taken from independent sources but on the reporting entity's own assumptions drawn from the assumptions that market participants would use, based on observables.

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

In case of availability of quoted market prices in active markets, an entity cannot follow a different approach than Level 1. Furthermore, the valuation techniques used should prioritise the utilisation of inputs observable in the market and should rely as little as possible on the reporting entity's own data, internal valuations or unobservable inputs.

### IOR fair value policy and fair value hierarchy

The fair values of investments held by the IOR quoted in active markets are usually based on current bid prices. A financial instrument is considered quoted in active markets if the prices are promptly and regularly available in an official list or from an authority and these prices represent effective market transactions that are regularly traded. If the market for a financial asset is not active or if the market at valuation time is not considered active, for instance in case of illiquid markets, the valuation

techniques adopted by IOR are based on the use of recent arm's length transactions, although not active, or in reference to the current fair value of a similar instrument. These evaluation techniques also include discounted cash flows analysis and other valuation techniques commonly used by market participants. If recent transactions on the same or similar instruments are not available, the IOR uses valuation techniques based on market parameters or other parameters. Utilising valuation techniques, the IOR tries to use observable market data, reducing its reliance on internal data. Valuation techniques are periodically reviewed and calibrated, assessing the quantity and the quality of information at the balance sheet date, in order to correctly reflect any changes in the market. For the same reason, adjustments to market inputs, utilised in a certain model, can change from time to time. Consequently IOR models are calibrated to ensure that outputs reflect actual data and comparative market prices.

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

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

Under Level 3, the IOR has classified equity securities that are not quoted or other financial instruments for which fair values are determined using a model based on internal parameters. To the extent that is practical, the models use only observable data. However, areas such as default rates, volatilities and correlations require the Directorate to make estimates.

In this category the Institute has also classified other financial instruments:

- for which the IOR did not receive independent valuations;
- for which the IOR has not had defined and updated financial information;
- for which, despite having defined and updated financial information, the Institute believes that the valuation of underlying assets, due to the nature of the investment, is based on valuation parameters that are not immediately observable on the market;
- for which the IOR has received an independent expert evaluation (for investment properties).

The table below sets out what is required under IFRS 13 in terms of levels of fair value, distinguishing between assets and liabilities measured at fair value on a recurring basis and on a non-recurring basis:

| | 2014 EUR 000 | | | |
|---|---|---|---|---|
| **RECURRING ITEMS** | *Fair Value* | *Level 1* | *Level 2* | *Level 3* |
| Trading securities | 1,718,136 | 1,676,950 | 5,246 | 35,940 |
| *Bonds and Debt securities* | *1,627,870* | *1,627,869* | *1* | – |
| *Equities* | *13,005* | *13,005* | – | – |
| *External Investment Funds* | *77,261* | *36,076* | *5,245* | *35,940* |
| Investment securities, equities Available for sale securities | 10,390 | 10,382 | – | 8 |
| Gold, medals and precious coins | 33,208 | 33,208 | – | – |
| Securities sold to be settled | – | – | – | – |
| Investment properties | 2,181 | – | – | 2,181 |
| **TOTAL RECURRING ITEMS** | **1,763,915** | **1,720,540** | **5,246** | **38,129** |

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

| | 2014 EUR 000 | | | | |
|---|---|---|---|---|---|
| **NON-RECURRING ITEMS (ASSETS)** | *Carrying Value* | *FairValue* | *Level 1* | *Level 2* | *Level 3* |
| Cash | 16,351 | 16,351 | 16,351 | – | – |
| Bank Deposits | 551,007 | 551,007 | 551,007 | – | – |
| Loans and advances to customers | 22,408 | 24,039 | – | – | 24,039 |
| Loans and receivables securities | 187,677 | 186,669 | – | 186,669 | – |
| Held to maturity securities | 645,054 | 688,050 | 688,050 | – | – |
| **TOTAL NON-RECURRING ASSETS** | **1,422,497** | **1,466,116** | **1,255,408** | **186,669** | **24,039** |
| **NON-RECURRING ITEMS (LIABILITIES)** | | | | | |
| Due to depositors | 2,361,863 | 2,361,863 | – | – | 2,361,863 |
| Due to banks | 16 | 16 | 16 | – | – |
| **TOTAL NON-RECURRING LIABILITIES** | **2,361,879** | **2,361,879** | **16** | **–** | **2,361,863** |

| | 2013 EUR 000 | | | |
|---|---|---|---|---|
| **RECURRING ITEMS** | *Fair Value* | *Level 1* | *Level 2* | *Level 3* |
| Trading securities | 1,748,901 | 1,504,656 | 201,872 | 42,373 |
| *Bonds and Debt securities* | *1,434,027* | *1,434,026* | *1* | – |
| *Equities* | *64,173* | *64,173* | – | – |
| *External Investment Funds* | *250,701* | *6,457* | *201,871* | *42,373* |
| Investment securities, equities Available for sale securities | 13,930 | 13,922 | – | 8 |
| Gold, medals and precious coins | 29,867 | 29,867 | – | – |
| Securities sold to be settled | 23 | 23 | – | – |
| Investment properties | 2,126 | – | – | 2,126 |
| **TOTAL RECURRING ITEMS** | **1,794,847** | **1,548,468** | **201,872** | **44,507** |

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

| | 2013 EUR 000 | | | | |
|---|---|---|---|---|---|
| **NON-RECURRING ITEMS (ASSETS)** | *Carrying Value* | *Fair Value* | *Level 1* | *Level 2* | *Level 3* |
| Cash | 38,784 | 38,784 | 38,784 | – | – |
| Bank Deposits | 677,206 | 677,206 | 677,206 | – | – |
| Loans and advances to customers | 29,462 | 31,463 | – | – | 31,463 |
| Loans and receivables securities | 250,870 | 249,243 | – | 249,243 | – |
| Held to maturity securities | 574,816 | 601,740 | 601,740 | – | – |
| **TOTAL NON-RECURRING ASSETS** | **1,571,138** | **1,598,436** | **1,317,730** | **249,243** | **31,463** |
| **NON-RECURRING ITEMS (LIABILITIES)** | | | | | |
| Due to depositors | 2,544,278 | 2,544,278 | – | – | 2,544,278 |
| Due to banks | 1 | 1 | – | – | 1 |
| **TOTAL NON-RECURRING LIABILITIES** | **2,544,279** | **2,544,279** | – | – | **2,544,279** |

**Annual variations of assets measured at fair value on a recurring basis assigned into Level 3.**
The following table provides information about the assets measured at fair value on a recurring basis and assigned to Level 3 of the fair value hierarchy, the initial stock, disposals and / or additions occurred during the year, and their final values at the closing date of the financial statements.

| | 2014 EUR 000 | | | 2013 EUR 000 | | |
|---|---|---|---|---|---|---|
| | *Investment Funds* | *Available for sale securities* | *Investment Property* | *Investment Funds* | *Available for sale securities* | *Investment Property* |
| Balance at 1 January | 42,373 | 8 | 2,126 | 144,360 | 8 | 1,914 |
| Additions | – | – | 73 | 64,799 | – | – |
| Unrealised Plus (Minus) recognised through profit or loss | (1,888) | – | (18) | (22,426) | – | 212 |
| Unrealised Plus (Minus) recognised through Other Comprehensive Income | – | – | – | – | – | – |
| Transfers from other levels | – | – | – | – | – | – |
| Sales | (4,276) | – | – | (138,288) | – | – |
| Realised Plus (Minus) recognised through profit or loss | (269) | – | – | 385 | – | – |
| Realised Plus (Minus) recognised through Other Comprehensive Income | – | – | – | – | – | – |
| Transfers to other levels | – | – | – | (6,457) | – | – |
| **Balance as of 31 December** | **35,940** | **8** | **2,181** | **42,373** | **8** | **2,126** |

**Disclosures about assets measured at fair value on a recurring basis**
In this paragraph we provide IFRS 13 disclosure requirements about assets measured at fair value on a recurring basis. By definition, the carrying value of these items corresponds to the fair value.
The fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. an exit price).

## TRADING SECURITIES

These consist of:

**Debt securities:** the Institute invested in debt securities valued at mark-to-market price and regularly traded in active, liquid markets. As a consequence, these instruments are in Level 1 of the fair value hierarchy, except for a bond classified as Level 2 in the portfolio amounting to EUR 1,000.

**Equity securities:** the Institute invested in equity securities valued at mark-to-market and regularly traded in active, liquid markets. As a consequence, these instruments are in Level 1 of the fair value hierarchy.

**Investments funds:** the investment of the Institute in external investment funds amounts to EUR 77.3 m. Except for EUR 36.1 m assigned to Level 1, representing securities waiting for reimbursement, investment funds are classified under Level 2 or Level 3 depending on NAV availability, the existence of listed or unlisted securities within the portfolio and commitments, the investment type (securities, real estate, equity, etc.) and / or limitations linked to exit clauses. As a consequence, at the end of 2014, a total of EUR 5.3 m was classified as Level 2, while the remaining amount for EUR 35.9 m was Level 3.

## INVESTMENT EQUITY SECURITIES, AVAILABLE FOR SALE

These are mainly classified as Level 1, being composed of shares quoted in active, liquid markets, excepted for an unlisted equity security for a small amount classified as Level 3.

## GOLD, MEDALS AND PRECIOUS COINS

Gold, medals and precious coins are valued at mark-to-market, regularly tradable in active, liquid markets. As a consequence, these instruments are in Level 1 of the fair value hierarchy.

## INVESTMENT PROPERTIES

This item comprises properties directly owned by the Institute. The fair value of the properties is assessed by a qualified, independent expert. The appraisal is based on real estate market research from the main sector experts, as well as official data. The parameters used also reflect expert assumptions based on available information. For these reasons, the investment properties are classified as being in Level 3 of the fair value hierarchy.

**Valuation techniques utilised to measure fair value (Level 2 and Level 3)**

All illiquid financial instruments or unlisted financial instruments with investments in listed instruments were classified as Level 2. The basis for the valuation of investments is pricing provided by the securities issuer. These prices are internally verified and tested using internal models and observable market parameters, and, if there are discrepancies, adjusted according to the above-mentioned analysis. They are also adjusted on the basis of valuations from independent sources. Non-listed funds or other financial instruments valued using models based, at least partially, on internal valuation parameters, were classified as Level 3. For the NAV of funds, the difference between the current value of the assets and liabilities of the fund, adjustments were made to include other risk factors.

The Fair Value Adjustment (FVA) is defined as a quantity to be added to the mid-price observed in markets, rather than the price issued to the model with the aim of obtaining the fair value of the position. The FVA includes the uncertainty during the evaluation of a financial instrument with the goal of: reducing the risk of including incorrect evaluations in the financial statements; ensuring

that fair value reflects the realised price of a market transaction that is actually possible; and incorporating possible future expenses. The Institute amended the value of financial instruments measured at fair value on a recurring basis classified as Level 2 and Level 3 based on credit risk (Credit Valuation Adjustment), liquidity risk related to the disinvestment and close-out costs.

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

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

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

For fair value measurements where significant unobservable inputs are used (Level 3), a sensitivity analysis is performed in order to obtain the range of reasonable alternative valuations. The Institute takes into account that the impact of unobservable inputs on the measurement of fair value of Level 3 depends on the correlation between the different inputs used in the valuation process. The sensitivity analysis was performed by carrying out a stress test on the PD and LGD by + / – 5 % and showed that the impacts are not significant for the portfolio measurement assigned into Level 3.

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

### CASH
Recorded at Level 1 of the fair value hierarchy. Due to the short-term nature and generally negligible credit risk, the carrying value of cash approximates fair value.

### BANK DEPOSITS
This item comprises deposits on demand and term deposits with banks. Assuming what was already explained in relation to the category "Cash" and assuming also that term deposits do not exceed ninety days, at the closing date of the financial statements, the carrying value of bank deposits approximates fair value and they were recorded in Level 1 of the fair value hierarchy.

### LOANS AND ADVANCES TO CUSTOMERS
This item comprises of all credits towards customers; particularly credit lines, loans and overdrafts. Referring to doubtful loans, considered non-collectible, for which the Institute proceeded with a specific impairment loss, the carrying value represents fair value. Referring to other credits, the fair value was calculated as follows:

- Loans and credit lines: calculated by discounting future flows based on a representative rate;
- Overdrafts: given their nature, the value of overdrafts approximates the fair value.

### LOANS AND RECEIVABLES SECURITIES

For this item, the fair value represents the market value at the closing date of the financial statements. By their nature "Loans and Receivables" securities are not quoted in active, liquid markets, but the evaluation is sent weekly by the counterpart and it is controlled with an internal model. For these reasons, "Loans and Receivables" are classified in Level 2 of the fair value hierarchy.

### HELD TO MATURITY SECURITIES

The fair value of Held to maturity securities corresponds to the market value at the closing date of the financial statements. The securities are in Level 1 of the fair value hierarchy since they are regularly traded on active, liquid markets.

**Liabilities not measured at fair value on a recurring basis**

### DUE TO DEPOSITORS

This item comprises customers' deposits on demand and term deposits, but also liquidity accounts and term deposits related to Asset Management positions. Their carrying value approximates fair value, considering the short maturity. The fair value calculation is based on parameters not observable on markets, not even indirectly, so Due to depositors is in Level 3 of the fair value hierarchy.

### DUE TO BANKS

The carrying value of this item is very low and approximates fair value, considering the short maturity. The fair value calculation is based on parameters not observable on markets, not even in an indirect way, so they are recorded in Level 3 of the fair value hierarchy.

**Transfers between Portfolios**

The amendments to IAS 39 and to IFRS 7 "Reclassification of financial assets" make it possible to reclassify certain financial assets, after their initial recognition, out of the Held for trading (HFT) and Available for sale (AFS) portfolios. In particular, those HFT or AFS financial assets that would have fit the definition specified by international accounting standards for the loan portfolio (if such assets were not classified as HFT or AFS respectively on initial recognition) may be reclassified if the entity intends, and is able, to hold them for the foreseeable future or until maturity. The IOR did not conduct transfers between portfolios in 2014.

## 28. MEASUREMENT CATEGORIES OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The following table provides information about the carrying amounts of individual classes of financial instruments within the measurement categories of financial assets and financial liabilities as defined in IAS 39 "Financial Instruments: recognition and measurement". Only those assets and liabilities which are financial instruments as defined in IAS 32 "Financial Instruments: presentation" are included in the table below, which causes certain balances to differ from those presented on the Balance Sheet.

| | *2014* | *2013* |
|---|---|---|
| | *EUR 000* | *EUR 000* |
| *Financial Assets* | | |
| **FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS** | | |
| Trading securities | 1,718,136 | 1,748,901 |
| Gold, medals and precious coins | 33,208 | 29,867 |
| Derivative financial instruments | – | – |
| | **1,751,344** | **1,778,768** |
| **FINANCIAL ASSETS AT AMORTISED COST** | | |
| Cash and Bank deposits | 567,358 | 715,990 |
| Loans and advances to customers | 22,408 | 29,462 |
| Loans and receivables securities | 187,677 | 250,870 |
| Held to maturity securities | 645,054 | 574,816 |
| Other assets | 7,072 | 7,418 |
| | **1,429,569** | **1,578,556** |
| **FINANCIAL ASSETS AVAILABLE FOR SALE** | | |
| Investment securities, equities available for sale | 10,390 | 13,930 |
| | **10,390** | **13,930** |
| **Total Financial Assets** | **3,191,303** | **3,371,254** |
| *Financial Liabilities* | | |
| **FINANCIAL LIABILITIES AT AMORTISED COST** | | |
| Due to banks | 16 | 1 |
| Due to depositors | 2,361,863 | 2,544,278 |
| Other liabilities | 26,369 | 33,227 |
| | **2,388,248** | **2,577,506** |
| **Total Financial Liabilities** | **2,388,248** | **2,577,506** |

## 29. IFRS 10 "CONSOLIDATED FINANCIAL STATEMENTS" IFRS 11 "JOINT ARRANGEMENTS" IFRS 12 "DISCLOSURE OF INTEREST IN OTHER ENTITIES"

The goal of IFRS 10 is to provide a single standard for the consolidated financial statement indicating control as the main basis for consolidation of all types of entities. IFRS 10 replaced IAS 27 "Consolidated and separated financial statement" and the interpretation of SIC 12 "Consolidation – Special purpose entities". IFRS 11 covers the accounting by entities that jointly control an arrangement and replaced IAS 31 "Joint venture participations" and SIC 13 "Jointly Controlled Entities – Non-Monetary contributions by ventures". IFRS 12 combines, enhances and replaces the disclosure requirements for subsidiaries, for agreements for joint control, for associates and for unconsolidated structured entities. The accounting standard IFRS 10 "Consolidated financial statements" outlines the requirements for the preparation and presentation of consolidated financial statements. IFRS 10 changes the prior definition of control. Control requires exposure or rights to variable returns and the ability to affect those returns through power over an investee.

According to IFRS 10 an entity has to present the consolidated financial statements when the following criteria are satisfied:

- power over the investee;
- exposure to the variability of returns due to the investee;
- ability to influence the returns of the investment.

The Institute does not provide for the preparation of consolidated financial statements. The Institute is required to give supplementary information on unconsolidated structured entities, as mandated by IFRS 12 "Disclosure of interests with other entities". The accounting standard established the information that the Institute is required to present in the financial statements about the unconsolidated structured entities. The goal of IFRS 12 is to require an entity to specify the information that allows the reader of the financial statements to value:

- the nature and the risks arising from the participations in other entities;
- the effects of such participations on its Balance Sheet, Income Statement and financial flows.

For unconsolidated structured entities the Institute considers the shares held in externally managed investment funds. For some of the external funds, the Institute is the owner of a significant number of shares, but does not control these funds because, since it does not participate in investment decisions, either directly or indirectly, it does not hold the ability to affect the returns of the above-mentioned funds. The information required by the accounting standard on the unconsolidated structured entities follows.

| | 2014 | | 2013 | |
|---|---|---|---|---|
| *Investment fund type* | *Balance sheet exposure* | | *Balance sheet exposure* | |
| | *Nominal value* | *Carrying amount (EUR)* | *Nominal value* | *Carrying amount (EUR)* |
| Open-end fund | 390,867 | 41,320,937 | 3,868,265 | 173,597,235 |
| Closed-end fund | 20,170,677 | 23,354,388 | 21,706,820 | 62,937,158 |
| Hedge fund | – | – | – | – |
| Exchange traded fund | – | – | – | – |
| Unit investment Trust | – | – | – | – |
| Fund of fund | 2,300 | 12,585,456 | 2,399 | 14,167,458 |
| Seed Fund | – | – | – | – |
| **Total** | **20,563,844** | **77,260,781** | **25,577,484** | **250,701,851** |

| *Underlying asset class focus* | *Balance sheet exposure* | | *Balance sheet exposure* | |
|---|---|---|---|---|
| | *Nominal value* | *Carrying amount (EUR)* | *Nominal value* | *Carrying amount (EUR)* |
| Equity | 92,212 | 23,097,413 | 2,069,579 | 165,866,212 |
| Debt | 292,960 | 30,167,668 | 2,256,498 | 50,289,311 |
| Asset allocation | – | – | 99 | 129,913 |
| Money Market | – | – | – | – |
| Real Estate | 20,170,000 | 23,332,751 | 21,170,000 | 28,047,140 |
| Commodity | – | – | – | – |
| Alternat. investments | 8,672 | 662,949 | 81,308 | 6,369,275 |
| **Total** | **20,563,844** | **77,260,781** | **25,577,484** | **250,701,851** |

| *Geographical Area* | *Balance sheet exposure* | | *Balance sheet exposure* | |
|---|---|---|---|---|
| | *Nominal value* | *Carrying amount (EUR)* | *Nominal value* | *Carrying amount (EUR)* |
| EU | 20,563,844 | 77,260,781 | 25,135,629 | 250,454,497 |
| USA | – | – | 441,855 | 247,353 |
| **Total** | **20,563,844** | **77,260,781** | **25,577,484** | **250,701,851** |

At the closing date of the financial statements, the Institute recorded EUR 77.3 m in investments in external funds in its trading portfolio.

50 % of funds are related to funds that can be subscribed to by different entities at any time and for any amount (open-end funds). Conversely 30 % of the funds in the portfolio are closed-end funds, and can be subscribed to only at given times by specific subjects, who, as mentioned, have no control. The remaining portion consists of funds that invest in other funds (16 %). With regard to the asset classes covered, the Institute holds shares of funds investing in Equity securities (30 %), Debt securities (39 %) and real estate market (30 %).

Regarding geographical area, the criteria used in the abovementioned table were to separate funds depending on their legally registered domicile. According to these criteria, all the funds are located within the European Union.

At the closing date of these financial statements, the Institute had a standing commitment with third parties of EUR 4 m. At the closing date of these financial statements, the IOR did not provide any guidance to unconsolidated structured entities on their investment policies. The Institute has not sponsored any unconsolidated structured entities. SGIR is 100 % owned by IOR. The Institute does not provide the preparation of the Consolidated financial statements because the resulting information would not be relevant to the reader of the financial statements. The total balance sheet assets of the subsidiary are insignificant when compared with those of the Institute and, accordingly, the consolidated financial statements would not differ significantly from these financial statements.

## 30. EXCHANGE RATES AS OF THE BALANCE SHEET DATE

The balances, existing at the year-end, denominated in the main currencies are valued at the exchange rates observed by the European Central Bank on the last working day of the year (in 2014: 30 December). For the other currencies, the rates used are those provided by Reuters on the same date.

For these statements the rates were determined as follows:

| Currency | | 2014 | 2013 |
|---|---|---|---|
| U.S. Dollars | USD | 1.216 | 1.3783 |
| Swiss Francs | CHF | 1.2028 | 1.2259 |
| Canadian Dollars | CAD | 1.4132 | 1.4764 |
| English Pounds | GBP | 0.7823 | 0.8364 |
| Australian Dollars | AUD | 1.4878 | 1.5520 |
| Japanese Yen | JPY | 145.41 | 145.02 |
| Czech Crowns | CZK | 27.728 | 27.48 |
| Danish Crowns | DKK | 7.4436 | 7.4603 |
| Hungarian Forints | HUF | 314.98 | 296.8 |
| Norwegian Crowns | NOK | 9.042 | 8.4255 |
| Polish Zloty | PLZ | 4.3103 | 4.1487 |
| Swedish Crowns | SEK | 9.4746 | 8.9283 |
| Argentinian Pesos | ARS | 8.9516 | 8.9516 |
| Brazilian Reais | BRE | 3.2394 | 3.2208 |
| Mexican Pesos | MXP | 17.9293 | 15.9586 |
| South African Rand | ZAR | 14.1487 | 14.4257 |
| Hong Kong Dollars | HKD | 9.434 | 10.6886 |
| South Korean Won | KRW | 1,334.19 | 1,454.26 |
| Singapore Dollars | SGD | 1.6085 | 1.7481 |
| New Zealand Dollars | NZD | 1.5536 | 1.6866 |

## 31. DATE OF AUTHORISATION FOR ISSUE

These financial statements were presented and authorised for issue by the Directorate on 2 March 2015 and approved by the Board of Superintendence on 31 March 2015.

## 32. EVENTS AFTER 31 DECEMBER 2014

No material events have occurred after the balance sheet date that would make it necessary to change any of the information given in these financial statements.

SECTION V



# Financial Risk Management

## 5.1 Strategy in using financial instruments

By their nature, the IOR's activities are principally related to the use of financial instruments. The Institute accepts deposits from customers at both fixed and floating rates, for various periods, and seeks to earn above-average interest margins by investing these funds in high quality assets. The Institute seeks to increase these margins by consolidating short-term funds and investing for longer periods at higher rates, while maintaining sufficient liquidity to meet any obligations that might fall due. Therefore, the IOR's activities expose it to a certain level of financial risk. The Institute sets appropriate risk limits and takes action to measure, manage and monitor the risk. The objective is to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Institute's financial performance.

The Institute's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls and to monitor the risk and adherence to limits by means of reliable and up-to-date information systems. For these purposes, a Risk Management Department was created in 2007, with a dedicated, specialised staff. This department analyses credit risks, market risks and operational risks. The following paragraphs detail the IOR's risk management approach, with regard to credit risk, market risk (interest rate risk, currency risk and other price risk), liquidity risk and capital requirements.

## 5.2 Credit Risk

The Credit Risk is the risk of loss resulting from the failure of a customer or counterparty to meet their contractual obligation. The objective of monitoring the credit risk is to recognise in a timely way those situations that give rise to an anomalous trend, so that the IOR can quickly define the corrective actions to be taken. Financial assets that potentially subject the Institute to concentrations of credit risk, comprise mainly bank deposits and debt securities.

The IOR manages its credit risk by monitoring actual credit exposures against defined credit and counterparty limits. Limits on the level of credit risk are approved by the Board of Superintendence, based on the proposal of Risk Management Department agreed by the Directorate and are subject to an annual review or every time there is some news about ratings changes that affect the defined risk ranges. A system called “Gestione Limiti Operativi Area Finanza” has been implemented. The approved limits for each counterparty, both as a single institution and as a group, are entered into the system at the start of each year, following the approval of the Board of Superintendence. At least once a day, the system produces a table with comparisons between the approved limits and the actual credit exposures.

The table below shows the concentration per rating of term deposits with banks.

TABLE 5.2.1 TERM DEPOSITS WITH BANKS BY RATING S&P

| | *2014* | *2013* |
|---|---|---|
| AAA | – | – |
| AA+ | – | – |
| AA | – | – |
| AA- | – | 28.20 % |
| A+ | – | 35.90 % |
| A | 34.63 % | – |
| A- | – | 26.34 % |
| BBB+ | 43.72 % | – |
| BBB | – | – |
| BBB- | – | 9.56 % |
| BB | 21.65 % | – |
| Not rated | – | – |
| **Total** | **100.00 %** | **100.00 %** |

Comparing the two years, there was a deterioration due to the risk deterioration of the financial institutions that are IOR counterparties for term deposits. The deterioration was also caused by the downgrading of most sovereign states, which impacted the counterparties' ratings.

The table below shows the distribution of ratings within the bond property portfolio, which comprises all interest-bearing securities, including trading securities and financial assets held to maturity, as well as Loans and Receivables.

TABLE 5.2.2 BOND PORTFOLIO BY RATING S&P

| | *2014* | *2013* |
|---|---|---|
| AAA | 11 % | 20 % |
| AA+ | 9 % | 11 % |
| AA | 4 % | 4 % |
| AA- | 2 % | 11 % |
| A+ | 5 % | 2 % |
| A | 10 % | 4 % |
| A- | 6 % | 4 % |
| BBB+ | 16 % | 3 % |
| BBB | 33 % | 26 % |
| BBB- | 2 % | 8 % |
| BB+ | – | 2 % |
| BB | – | 5 % |
| BB- | 2 % | – |
| **Total** | **100 %** | **100 %** |

Within the bond portfolio, the rating deterioration also depended on the downgrading of sovereign debt risks (mainly Italian) and to the subsequent downgrading of bond issuers from the downgraded countries.

As far as the Credit Risk on Loans and advances to customers is concerned, the IOR judges that it is not necessary to be equipped with special systems to measure the risk because:



- the item is immaterial compared to the IOR's total assets;
- counterparties are religious congregations or institutions or Vatican employees, which are categories with a low risk profile;
- the IOR generally obtains collateral for funds advanced, such as securities or managed assets or, in the case of employees of the IOR, termination indemnity. As of 31 December 2014, this collateral amounted to EUR 4.2 m.

In any case, Customer Credit Risk is monitored by utilising information and procedures for assessing the sustainability of the loans.

An internal monitoring tool helps the Directorate to determine whether objective evidence of impairment exists on loans to customers, based on the following criteria set out by the Institute:

- delinquency in contractual payments of principal or interest;
- cash flow difficulties experienced by the borrower;
- deterioration in the value of collateral.

At the end of each month, the Loan Department analyses all credits, and if there are positions past due and uncollectible, it asks the Directorate to write off the whole amount as a credit loss. If the past due position is thought to be collectible but not in the short term, the credit is individually impaired. If the past due position is thought collectible in the short term, it is not individually impaired, but the department monitors the situation.

TABLE 5.2.3 LOANS QUALITY

| | 2014<br>EUR 000 | | | |
|---|---|---|---|---|
| | *N.* | *Gross amount* | *Impairment* | *Carrying amount* |
| Performing loans | 379 | 25,296 | 5,856 | 19,440 |
| Restructured loans | – | – | – | – |
| Past due but not impaired | 2 | 80 | 5 | 75 |
| Analytically impaired | 16 | 13,315 | 10,422 | 2,893 |
| **Total** | **397** | **38,691** | **16,283** | **22,408** |

| | 2013<br>EUR 000 | | | |
|---|---|---|---|---|
| | *N.* | *Gross amount* | *Impairment* | *Carrying amount* |
| Performing loans | 450 | 28,978 | 4,808 | 24,170 |
| Restructured loans | 9 | 1,734 | 104 | 1,630 |
| Past due but not impaired | – | – | – | – |
| Analytically impaired | 11 | 12,422 | 8,760 | 3,662 |
| **Total** | **470** | **43,134** | **13,672** | **29,462** |

Below is a breakdown of the item "Loans to customers".

TABLE 5.2.4 LOANS TO CUSTOMERS

| | *2014* | *2013* |
|---|---|---|
| Clergy, religious congregations and other ecclesial bodies | 40.96 % | 31.60 % |
| IOR and Vatican City State employees | 56.44 % | 64.73 % |
| Various | 2.60 % | 3.67 % |
| | **100.00 %** | **100.00 %** |

The IOR also issued guarantees requested by customers covered by assets held in custody, which are disclosed in Section IV, note 24.

## 5.3 Geographical concentration of assets, liabilities

The IOR has credit exposure mainly through its bond portfolios, with issuers domiciled all around the world, and to banks domiciled outside of the Vatican City State. High geographical concentration is a risk factor if there is a country risk. Country risk is the risk arising from country-specific events. The objective of monitoring the concentration risk is to quickly recognise those situations that may indicate anomalous behaviour, so that the IOR can quickly define the corrective actions to be taken. The concentration risk is measured by allocating all assets and liabilities based on the country of domicile of its counterparties.

The geographical analysis of assets and liabilities items based on the domicile of the counterparties is set out in the following table:

TABLE 5.3.1

| | *2014* | | *2013* | |
|---|---|---|---|---|
| | *EUR 000* | | *EUR 000* | |
| | *Total Assets* | *Total Liabilities* | *Total Assets* | *Total Liabilities* |
| Vatican City State | 62,844 | 1,018,478 | 51,273 | 1,033,839 |
| Italy | 801,479 | 1,122,870 | 694,317 | 1,296,214 |
| Spain | 464,206 | 15,755 | 220,209 | 10,623 |
| Holland | 187,389 | 522 | 334,633 | 406 |
| Germany | 173,668 | 4,050 | 314,319 | 4,047 |
| France | 163,951 | 11,501 | 149,527 | 10,326 |
| Great Britain | 140,171 | 1,438 | 92,260 | 1,518 |
| Ireland | 72,833 | 2,117 | 49,825 | 2,015 |
| Sweden | 65,113 | 98 | 51,880 | 1 |
| Luxembourg | 57,816 | 656 | 210,658 | 827 |
| Other European Countries | 194,123 | 63,878 | 456,111 | 63,072 |
| USA and Canada | 484,181 | 9,882 | 367,229 | 8,883 |
| Other countries | 288,291 | 227,273 | 336,086 | 195,650 |
| Remaining assets or liabilities | 54,710 | 37,263 | 62,690 | 43,549 |
| **Total** | **3,210,775** | **2,515,781** | **3,391,017** | **2,670,970** |

No other countries represent more than 2 % of total assets.

TABLE 5.3.2 EXPOSURE TO GREECE, IRELAND, ITALY, PORTUGAL, SPAIN

| | *2014* | | *2013* | |
|---|---|---|---|---|
| | *EUR 000* | | *EUR 000* | |
| | *Total Assets* | *Total Liabilities* | *Total Assets* | *Total Liabilities* |
| Greece | – | 602 | – | 621 |
| Ireland | 72,833 | 2,117 | 49,825 | 2,015 |
| Italy | 801,479 | 1,122,870 | 694,317 | 1,296,214 |
| Portugal | 9,857 | 3,074 | 122,221 | 2,653 |
| Spain | 464,206 | 15,755 | 220,209 | 10,623 |
| **Total** | **1,348,375** | **1,144,418** | **1,086,572** | **1,312,126** |

## 5.4 Market Risk

The Market Risk is the risk that the fair value or future cash flows of a financial instrument fluctuate because of changes in market variables.

Market risk is comprised of the following three types of risk:

- currency risk (the risk that the fair value or future cash flows of a financial instrument fluctuate because of changes in foreign exchange rates);
- interest rate risk (the risk that the fair value or future cash flows of a financial instrument fluctuate because of changes in market interest rates);
- other price risk (for individual financial instruments or for all similar financial instruments).

The IOR has exposure to market risks. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to both general and specific market factors. General market risk factors include interest rates, equity index levels, exchange rates, commodity prices and general credit spreads. The volatility of these risk factors and the correlations between them are also general market risk factors. Specific components relate to the prices of debt and equity instruments which result from factors and events specific to individual companies or entities. The objective of monitoring market risk is to understand and manage market risk, in order to be able to face any extreme events affecting the three areas mentioned above.

### 5.4.1. Main risk management indicators of the property portfolio

The IOR applies a "Value at risk" methodology to estimate the market risk of positions held, and the maximum losses expected based on a number of assumptions for various changes in market conditions.

The Risk Management Department provided the following information about risk analysis.

The Department analysed the property portfolio and the term deposits with banks using the Bloomberg PORT risk analysis software. We enclose some brief explanatory notes detailing the analysis methods, and we define the main risk indicators used:

- the IOR uses the Monte Carlo simulations model, which accounts for a wide range of possible future risks, looking at the historical correlation between all the involved variables;
- Modified Duration measures prices sensitivity to yield;
- the Value at Risk (VaR) is the sum of the possible losses in a one-day period, associated with negative market trends, with a confidence level of 99 %. It quantifies the exposure to market risk, or the risk that a position declines in value with adverse market price changes;
- the Expected Shortfall (ES) is the average of VaR values in a one-month period for all confidence levels between 99 % and 100 %. It defines the average worst-case scenario.

The following table, prepared by the Risk Management Department, refers to December 2014.

*As of 30 December 2014*

| *Indicator* | *Trading Securities, Cash and Demand accounts* | *HTM, L&R and Term Deposits* | *Total Portfolio* |
|---|---|---|---|
| Market Value | 2,111,862,624 | 1,049,021,456 | 3,160,884,080 |
| Modified Duration | 1,48 | 2,02 | 1,66 |
| Value at Risk (99 % CL, Horizon period 1d MC Simulations) | 6,470,005 | 1,530,603 | 7,279,118 |
| Expected Shortfall | 8,325,831 | 1,851,648 | 9,366,908 |

## 5.4.2 Currency risk

**Concentration of assets, liabilities and off balance sheet items**



The Institute is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial positions and cash flows. The objective of monitoring currency risk is to achieve an appropriate balance between return and risk arising from unmatched liabilities and assets in currencies different from the base currency. The table below summarises the Institute's exposure to foreign currency exchange risk on 31 December 2014 and 2013. Included in the table are the Institute's assets and liabilities at carrying amounts categorised by currency. Although the Euro is not subject to currency risk, the relevant column has been left in to reconcile the total with the Balance Sheet presented in Section 1.

| *As at 31 December 2014* | | | | *EUR 000* | | | |
|---|---|---|---|---|---|---|---|
| | *EUR* | *USD* | *CAD* | *CHF* | *AUD* | *Other* | *Total* |
| **ASSETS** | | | | | | | |
| Cash and Bank Deposits | 387,013 | 145,513 | 10,258 | 4,334 | 6,359 | 13,881 | 567,358 |
| Trading securities | 1,176,709 | 531,054 | 2,710 | 2,308 | 3,171 | 2,184 | 1,718,136 |
| Gold, medals and precious coins | 11,080 | 22,128 | – | – | – | – | 33,208 |
| Derivative financial instruments | – | – | – | – | – | – | – |
| Loans and advances to customers | 22,152 | 256 | – | – | – | – | 22,408 |
| Loans and receivables securities | 162,416 | 25,261 | – | – | – | – | 187,677 |
| Investment securities, equities available for sale | 10,390 | – | – | – | – | – | 10,390 |
| Held to maturity securities | 606,530 | 38,524 | – | – | – | – | 645,054 |
| Investment in subsidiaries | 15,835 | – | – | – | – | – | 15,835 |
| Investment properties | 2,181 | – | – | – | – | – | 2,181 |
| Remaining other assets | 6,335 | 2,065 | 15 | 5 | 8 | 100 | 8,528 |
| **Total Assets** | **2,400,640** | **764,802** | **12,983** | **6,647** | **9,538** | **16,165** | **3,210,775** |
| **LIABILITIES** | | | | | | | |
| Due to banks | – | 16 | – | – | – | – | 16 |
| Due to depositors | 1,562,518 | 756,262 | 12,221 | 7,175 | 9,118 | 14,569 | 2,361,863 |
| Other liabilities | 22,442 | 7,302 | 148 | 3 | 2 | 58 | 29,955 |
| Post employment benefit plans | 123,947 | – | – | – | – | – | 123,947 |
| **Total Liabilities** | **1,708,907** | **763,580** | **12,369** | **7,178** | **9,120** | **14,627** | **2,515,781** |
| EQUITY | 694,994 | – | – | – | – | – | 694,994 |
| **Net currency position** | **(3,261)** | **1,222** | **614** | **(531)** | **418** | **1,538** | **–** |
| Off balance sheet net notional position | – | – | – | – | – | – | – |
| **Total Net currency position** | **(3,261)** | **1,222** | **614** | **(531)** | **418** | **1,538** | **–** |

| *As at 31 December 2013* | | | | *EUR 000* | | | |
|---|---|---|---|---|---|---|---|
| | *EUR* | *USD* | *CAD* | *CHF* | *AUD* | *Other* | *Total* |
| Total assets | 2,493,559 | 736,340 | 105,465 | 6,912 | 18,884 | 29,857 | 3,391,017 |
| Total liabilities | 1,774,731 | 736,547 | 105,191 | 6,607 | 18,881 | 29,013 | 2,670,970 |
| Equity | 720,047 | – | – | – | – | – | 720,047 |
| **Net currency position** | **(1,219)** | **(207)** | **274** | **305** | **3** | **844** | **–** |
| Off balance sheet net notional position | – | – | – | – | – | – | – |
| **Total Net currency position** | **(1,219)** | **(207)** | **274** | **305** | **3** | **844** | **–** |

### 5.4.3 Interest rate risk

**Interest sensitivity of assets, liabilities and off balance sheet items**
Interest rate risk is the exposure of a bank to unfavourable changes in market interest rates. Interest rate risk is the potential negative impact of changes in market interest rates on performances of financial assets and financial liabilities that reach their maturity during a certain period, creating cash flows to be reinvested at the new market conditions, or that have to be repriced. The assumption of such risk is core to the banking business and is an important source of return and asset values. Nevertheless, an excessive interest rate risk may have adverse effects on financial performance and on the equity of a financial institution. Changes in interest rates affect the economic result as they increase or decrease the interest margin and the net trading income, which are sensitive to interest rates. Changes in interest rates also affect the value of assets, liabilities and off-balance sheet items as the future expected cash flows change with interest rates. Therefore, an effective risk management system that keeps the appropriate interest risk exposure is essential for the safety of a financial institution. Hence, the objective of interest rate risk management is to maintain profits, to improve the ability to absorb potential losses, and to ensure adequate rewards for the risk taken on. The management of interest rate risk aims to measure the risks arising from maturities and repricing mismatches, and is measured both from the earnings and economic value perspective. The Institute has exposure to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows.

The table below summarises the Institute's exposure to interest rate risks.

Included in the table are the Institute's assets and liabilities at carrying amounts, based on the date of contractual repricing or maturity dates. The off-balance sheet gap represents the net notional amounts of all interest-rate sensitive derivative financial instruments.

| *As at 31 December 2014* | | | | *EUR 000* | | | |
|---|---|---|---|---|---|---|---|
| | *Up to 1 month* | *1 – 3 months* | *3 – 12 months* | *1 – 5 years* | *Over 5 years* | *Non-interest* | *Total* |
| **ASSETS** | | | | | | | |
| Cash and Bank Deposits | 413,295 | 51,005 | 51,707 | 35,000 | – | 16,351 | 567,358 |
| Trading securities | 150,036 | 373,148 | 412,755 | 564,005 | 168,638 | 49,554 | 1,718,136 |
| Gold, medals and precious coins | – | – | – | – | – | 33,208 | 33,208 |
| Derivative financial instruments | – | – | – | – | – | – | – |
| Loans and advances to customers | 22,408 | – | – | – | – | – | 22,408 |
| Loans and receivables securities | 52,301 | 66,896 | 68,480 | – | – | – | 187,677 |
| Investment securities, equities available for sale | – | – | – | – | – | 10,390 | 10,390 |
| Held to maturity securities | 1,733 | 5,479 | 217,948 | 394,414 | 25,480 | – | 645,054 |
| Investment in subsidiaries | – | – | – | – | – | 15,835 | 15,835 |
| Investment properties | – | – | – | – | – | 2,181 | 2,181 |
| Remaining other assets | – | – | – | – | – | 8,528 | 8,528 |
| **Total Assets** | **639,773** | **496,528** | **750,890** | **993,419** | **194,118** | **136,047** | **3,210,775** |
| **LIABILITIES** | | | | | | | |
| Due to banks | 16 | – | – | – | – | – | 16 |
| Due to depositors | 2,202,342 | 7,322 | 152,199 | – | – | – | 2,361,863 |
| Other liabilities | 175 | – | – | – | – | 29,780 | 29,955 |
| Post employment benefit plans | – | – | – | – | – | 123,947 | 123,947 |
| **Total Liabilities** | **2,202,533** | **7,322** | **152,199** | **–** | **–** | **153,727** | **2,515,781** |
| **Off balance sheet net interest sensitivity gap** | – | – | – | – | – | – | |
| Interest sensitivity gap | (1,562,760) | 489,206 | 598,691 | 993,419 | 194,118 | (17,680) | |
| **Cumulative Interest sensitivity gap** | **(1,562,760)** | **(1,073,554)** | **(474,863)** | **518,556** | **712,674** | | |

| *As at 31 December 2013* | | | | | | | |
|---|---|---|---|---|---|---|---|
| Total assets | 961,394 | 445,222 | 365,394 | 915,107 | 450,999 | 252,899 | 3,391,017 |
| Total liabilities | 2,214,480 | 96,529 | 132,325 | 100,945 | – | 126,691 | 2,670,970 |
| Off balance sheet net interest sensitivity gap | – | – | – | – | – | – | |
| **Cumulative Interest sensitivity gap** | **(1,253,085)** | **(904,392)** | **(671,322)** | **142,840** | **593,839** | | |

## 5.5 Liquidity risk

**Maturities of assets and liabilities**
Liquidity risk is the risk that an entity will encounter difficulties in meeting obligations associated with financial liabilities when they are contractually due. The objective of monitoring liquidity risk is to prevent the Institute from being unable to meet obligations to repay depositors.

The IOR liquidity management process includes:

a) day-to-day funding, managed by monitoring future cash flows to ensure that requirements can be met. The IOR maintains an active presence in global money markets to enable this to happen;
b) maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
c) monitoring Balance Sheet liquidity ratios;
d) managing the concentration and profile of debt maturities.

The starting point for the liquidity measurement is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets.

| *As at 31 December 2014* | | | | *EUR 000* | | |
|---|---|---|---|---|---|---|
| | *Up to 1 month* | *1 – 3 months* | *3 – 12 months* | *1 – 5 years* | *Over 5 years* | *Total* |
| **ASSETS** | | | | | | |
| Cash and Bank Deposits | 429,647 | 51,004 | 51,707 | 35,000 | – | 567,358 |
| Trading securities | 60,711 | 132,027 | 403,137 | 887,046 | 235,215 | 1,718,136 |
| Gold, medals and precious coins | 33,208 | – | – | – | – | 33,208 |
| Derivative financial instruments | – | – | – | – | – | – |
| Loans and advances to customers | 5,975 | 464 | 1,444 | 4,136 | 10,389 | 22,408 |
| Loans and receivables securities | 1,301 | 66,896 | 33,482 | 85,998 | – | 187,677 |
| Investment securities, equities available for sale | 10,390 | – | – | – | – | 10,390 |
| Held to maturity securities | 1,732 | 1,425 | 68,551 | 547,866 | 25,480 | 645,054 |
| Investment in subsidiaries | – | – | – | – | 15,835 | 15,835 |
| Investment properties | – | – | – | – | 2,181 | 2,181 |
| Remaining other assets | 8,528 | – | – | – | – | 8,528 |
| **Total Assets** | **551,492** | **251,817** | **558,321** | **1,560,046** | **289,100** | **3,210,775** |
| **LIABILITIES** | | | | | | |
| Due to banks | 16 | – | – | – | – | 16 |
| Due to depositors | 2,202,341 | 7,323 | 152,199 | – | – | 2,361,863 |
| Other liabilities | 29,955 | – | – | – | – | 29,955 |
| Post employment benefit plans | 123,947 | – | – | – | – | 123,947 |
| **Total Liabilities** | **2,356,259** | **7,323** | **152,199** | **–** | **–** | **2,515,781** |
| **Net liquidity gap** | (1,804,767) | 244,494 | 406,122 | 1,560,046 | 289,100 | 694,994 |

| *As at 31 December 2013* | | | | | | |
|---|---|---|---|---|---|---|
| Total assets | 1,006,607 | 37,357 | 396,768 | 1,432,913 | 517,373 | 3,391,017 |
| Total liabilities | 2,341,171 | 96,529 | 132,325 | 100,945 | – | 2,670,970 |
| **Net liquidity gap** | **(1,334,563)** | **(59,172)** | **264,443** | **1,331,968** | **517,373** | **720,047** |

The table analyses the assets and liabilities of the Institute by relevant maturity groupings, based on the remaining period at balance sheet date to the contractual maturity date. The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Institute. It is unusual for financial institutions to be completely matched since business transactions often have an uncertain duration and vary in type. An unmatched position potentially enhances profitability, but can also increase the risk of losses. The maturities of assets and liabilities and the ability to replace, at acceptable costs, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Institute and its exposure to changes in interest rates and exchange rates.

## 5.6 Capital management

The Institute's objectives in managing capital, which is a broader concept than the "equity" shown in the balance sheet, are:

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

Capital adequacy and the use of capital are monitored daily. At the end of each day, the system automatically produces a table in which the net profit at the date is calculated, including also the annual changes in the Fair Value reserve of investment securities, equities Available for Sale. If their fair value decreases, its trend must be monitored, so that the IOR does not risk using capital reserves to cover this decrease, even if the result at the date is positive.

On a monthly basis, the Accounting Department produces a report in which the capital is divided into two tiers:

Tier 1: equity reserves, retained earning reserve and result for the period less potential dividends. If unrealised losses arise on the fair valuation of equity instruments held as available for sale, the relevant amount must be deducted. Unrealised actuarial losses on post-employment benefit are also deducted. Intangible assets are deducted.

Tier 2: Tier 1 plus unrealised gains arising on the fair valuation of equity instruments held as available for sale, adjusted with negative prudential filter for an amount of 50 %.

TABLE 5.6.1 CAPITAL

| | 2014 | 2013 |
|---|---|---|
| | EUR 000 | EUR 000 |
| **TIER 1** | | |
| Equity reserves | 309,874 | 309,874 |
| Retained earnings reserve | 357,426 | 409,561 |
| Fair value reserve (if<0) | – | – |
| Actuarial gain (loss) reserve (if<0) | (41,639) | (7,621) |
| Result of the year | 69,333 | 2,865 |
| Potential dividends | (55,000) | (55,000) |
| Intangible assets | (833) | (1,099) |
| **Total Tier 1** | **639,161** | **658,580** |
| **TIER 2** | | |
| Fair value reserve (if>0) | – | 5,368 |
| Negative prudential filter | – | (2,684) |
| **Total Tier 2** | **–** | **2,684** |
| **Total Capital** | **639,161** | **661,264** |

On 23 December 2014 Regulation n.1 of the Financial Intelligence Authority (AIF) was released, and it entered into force on 13 January 2015, the same date of the publication. The Regulation provisions IOR to comply with capital requirements. The Risk Management Department calculates the internal capital requirements to face the credit risk, the market risk and the operational risk and provides the following table to the Board of Superintendence. The table below summarises the Institute's internal capital requirements on 31 December 2014. As demonstrated below, the IOR is very highly capitalised.

CAPITAL REQUIREMENTS AND SOLVENCY RATIO

*62,530* + *100,986* + *12,898* = *176,414*

| *Credit Risk* | *Market Risk* | *Operational Risk* | *Minimum Capital Requirement* (based on solvency ratio of 8 %) |
|---|---|---|---|
| 62,530 | 100,986 | 12,898 | 176,414 |

$$\frac{639{,}161}{781{,}626 + 1{,}262{,}324 + 161{,}228} = $$

*28,98 % Tier 1 Ratio and Total Capital Ratio*

CHAPTER 11

# Report of the Board of Statutory Auditors



To the Board of Superintendence of the IOR,
The Board of Statutory Auditors, in accordance with article 28 of the Statute of the Istituto per le Opere di Religione (IOR), has reviewed the IOR's 2014 Annual Report prepared by the Management, which includes the Financial Statements composed of:

- Balance Sheet
- Income Statement
- Comprehensive Income Statement
- Cash Flows Statement
- Statement of Changes in Equity

The Annual Report also includes a description of the Institute's activity, a summary of significant accounting policies, critical accounting estimates and judgments, explanatory notes to the Financial Statements and information on financial risk management.

For the year ended 31 December 2014, the IOR's Financial Statements can be summarised as follows:

| | *EUR 000* |
|---|---|
| **BALANCE SHEET** | |
| Total Assets | 3,210,775 |
| Total Liabilities | 2,515,781 |
| Net Equity | 694,994 |
| **INCOME STATEMENT** | |
| Net Operating Result | 75,640 |
| Net Profit of The Year | 69,333 |
| Available for Distribution | 55,000 |

An independent audit of the IOR's Financial Statements as of 31 December 2014 has been completed by the External Auditors, Deloitte & Touche S.p.A, who expressed a clean opinion on 30 March 2015.
On the basis of the work done by this Board of Statutory Auditors during the year, in accordance with article 27 of the Statute, taking into account the conclusion made by the Internal Control functions of the IOR and considering the clean opinion issued by Deloitte & Touche S.p.A., we recommend to the Board of Superintendence to approve the 2014 Financial Statements, as proposed by the Management, and included in the Annual Report.

Furthermore, we agree to the Board of Superintendence proposal about the destination of the Net Profit of the year, which permits a provision of EUR 14,333 thousands to the Retained Earnings Reserve, allowing the IOR to transfer EUR 55,000 thousands to the Holy See, subject to the approval of the Commission of Cardinals.

Vatican City State, 30 March 2015

For the Board of Statutory Auditors
Mario M. Busso – President

CHAPTER 12

# Report of the External Auditors

Deloitte & Touche S.p.A.
Via della Camilluccia, 589/A
00135 Roma
Italia

Tel: +39 06 367491
Fax: +39 06 36749282
www.deloitte.it

## INDEPENDENT AUDITOR'S REPORT

**To the Members of the Superintendence Board of**
**ISTITUTO PER LE OPERE DI RELIGIONE**

### Report on the Financial Statements

We have audited the accompanying financial statements (Chapter 10 of 2014 Annual Report) of Istituto per le Opere di Religione, which comprise the balance sheet as at December 31, 2014, and the income statement, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### Management's Responsibility for the Financial Statements

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

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Ancona Bari Bergamo Bologna Brescia Cagliari Firenze Genova Milano Napoli Padova
Palermo Parma Roma Torino Treviso Verona

Sede Legale: Via Tortona, 25 - 20144 Milano - Capitale Sociale: Euro 10.328.220,00 i.v.
Codice Fiscale/Registro delle Imprese Milano n. 03049560166 - R.E.A. Milano n. 1720239
Partita IVA: IT 03049560166

Member of Deloitte Touche Tohmatsu Limited

**Opinion**

In our opinion, the financial statements present fairly, in all material respects, the financial position of Istituto per le Opere di Religione as at December 31, 2014, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

DELOITTE & TOUCHE S.p.A.

Enrico Ciai
Partner

Rome, Italy
March 30, 2015

Jean-Baptiste Douville de Franssu
President of the Board of Superintendence
Istituto per le Opere di Religione
Cortile Sisto V
00120 Città del Vaticano
Stato della Città del Vaticano
info@ior.va

**IOR – Istituto per le Opere di Religione**
Città del Vaticano, www.ior.va