dskbank
otp group

Head Office
Financing and Planning Division

YEAR END DISCLOSURE

In connection with the requirements of
Art. 335 of Ordinance No. 8 on the Capital Adequacy
of Credit Institutions

consolidated

2011

DSK Bank EAD as the former State Savings Bank was incorporated on 2 March 1951 in Bulgaria as a centralised deposit accepting institution. Since 1998, when the Act on DSK transformation has been passed, DSK Bank EAD (The Bank) was transformed into a commercial bank and is allowed to conduct all the transactions stated in art.1, par.2 from the Banking Law. Later the Bank receives a full banking license to operate as a commercial bank (by order No. 220882 of 26 September 2002 issued by the Bulgarian National Bank).

On 26 January 1999 Sofia City Court registered the State Savings Bank as a solely owned joint stock company "DSK Bank", 100% owned by the state. In 2001, pursuant to a court decision the Bank has been transformed to a joint stock company with its capital divided between the Council of Ministers –75%, and the Bank Consolidation Company AD – 25 %.

On 29 November 2002 following a decision of the Sofia City Court the Bank Consolidation Company acquired 100% of the share capital of DSK Bank EAD.

On 29 October 2003 following a decision of the Sofia City Court OTP Bank, incorporated in Hungary, acquired 100% of the share capital of DSK Bank EAD.

I. Capital Management and Capital Requirements of DSK Bank

Current consolidated disclosure is published according to art. 335 of Ordinance No. 8 of BNB on the Capital Adequacy of Credit Institutions (Ordinance 8). According to art. No. 335, par. 5 of Ordinance 8 an equivalent disclosure of non-disclosed here parts of Appendix 11 of the Ordinance is made in the Consolidated Financial Statements of the Bank.

The Management board of DSK Bank allocates the capital amongst various banking activities by maintaining a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position. The Bank Asset and Liabilities Committee reviews the level and trend of credit, market and operational risks and their effects on capital levels on a regular basis. Together with OTP Bank Hungary the Bank Group's risk profile is assessed in order to determine whether the Bank Group holds sufficient capital against the various risks and to assess future capital requirement either for regulatory purposes or from the internal understanding for its risk profile coverage according to its strategy.

1. Regulatory Capital Requirements

Bulgarian National Bank as the local regulatory authority sets out the general requirements regarding the amount, elements and structure of the total own funds for solvency purposes and of the minimum capital requirements to cover the risks taken by DSK Bank Group (the Bank Group). Capital adequacy compliance is monitored by the regulator on a semi-annual basis.

The Authority requires each bank or banking group to hold the minimum amount of or above the sum total of the capital requirements for:

- credit and dilution risk in the banking book;
- position risk in the trading book;
- counterparty and settlement risk from the entire activity;
- exchange rate and commodity risk from the entire activity and
- operational risk from the entire activity.

(1) Regulatory capital

Total own funds for solvency purposes are managed into two tiers:

Tier I (Primary) capital: paid-up share capital, reserves accumulated from profits after taxation and financial instruments without term that fulfil specific conditions. The book value of intangible assets including good will and unrealised losses arising from the fair valuation of financial instruments held as available for sale are deducted.

Tier II (Additional): capital: revaluation reserves from premises used for banking activity and qualifying subordinated term debt capital and hybrid debt capital instruments.

Deductions from regulatory capital are: (1) holdings in other credit and financial institutions, which are not consolidated and are amounting to more than 10% of their capital, (2) participations held in insurance undertakings, reinsurance undertakings and insurance holding companies amounting to 20% or more than 20 % of their capital, (3) country-specific deductions: holdings in non-financial institutions, which are not consolidated and are amounting to more than 10 % of their capital and (4) specific provisions for credit risk according to Ordinance 9 of BNB on the evaluation and classification of risk exposures of banks and the allocation of specific provisions for credit risk.. The deductions are made 50 % from Tier I and 50 % from Tier II capital.

Bulgarian National Bank defines the scope of consolidation for regulatory purposes. DSK Bank group has fully consolidated the following subsidiaries: DSK Asset Management, DSK Rodina Pension Company, DSK BUL Project, DSK Tours and its subsidiary DSK Trans Security which provides services auxiliary to the main banking activities as per the Credit Institutions Act. Equity consolidation is applied to the following associates: DSK Leasing and Cash Services Company.

Bulgarian National Bank sets out limits and ratios to regulatory capital and capital adequacy based on the guidelines developed by the Basel Committee and the European Community Directives. At any given time Tier II capital should not exceed Tier I capital. Tier II capital originating from hybrid debt capital instruments or subordinated term debt should not exceed 50% of Tier I capital.

(2) *Capital ratios*

Total own funds for solvency purposes

In thousands of BGN	**31 December 2011**	**31 December 2010**
Original own funds	**1 104 247**	**1 104 945**
Paid up capital	153 984	153 984
Reserves	960 686	960 686
Minority interests	1 242	1 162
Valuation differences in AFS debt securities	(2 745)	(1 016)
Funds for general banking risks	21 994	21 994
Intangible assets	(30 914)	(31 865)
Additional own funds	**306 316**	**443 098**
Revaluation reserves from premises used for banking activity	71 616	71 490
Subordinated Debt - maximum 50% of Original own funds	234 700	371 608
Deductions from original and additional own funds	**(52 753)**	**(3 064)**
Holdings in other credit and financial institutions amounting to more than 10% of their capital	(416)	(685)
Country-specific deductions from original and additional own funds	(2 410)	(2 379)
Specific provisions	(49 927)	-
Equal distribution of deductions		
Of which: from original own funds	(26 377)	(1 532)
Of which: from additional own funds	(26 376)	(1 532)
Total original own funds for general solvency purposes	**1 077 870**	**1 103 413**
Total additional own funds for general solvency purposes	**279 940**	**441 566**
Total own funds for solvency purposes	**1 357 810**	**1 544 979**
Surplus (+) / Deficit (-) of own funds compared to minimum requred	**575 480**	**768 519**

The Bank Group calculates the total capital adequacy (the 'Basel ratio') as a ratio between total own funds for solvency purposes and the total of the risk-weighted assets for credit, market and operational risks. Tier I capital adequacy is the ratio between the Tier I capital and the risk-weighted assets and should be higher than 6 %. The total capital adequacy ratio for Bulgaria should be higher than 12 % while the Basel ratio level is 8 %.

Capital Ratios

	31 December 2011	**31 December 2010**
Solvency ratio (%)	20.83%	23.88%
Original own funds ratio (%)	16.53%	17.05%

OTP Financing Netherlands B.V. granted two loan facilities in the form of subordinated term debt. The loan granted on 19.12.2007 amounts to 200 million euro and the loan granted on 20.10.2008 amounts to 150 million euro. To qualify as Tier II capital the subordinated term debt should meet regulatory requirements set out in the local Ordinance for capital adequacy of the credit institutions. The Bulgarian National Bank confirmed that these loan facilities meet the requirements and granted permission to DSK Bank to include them in the capital for regulatory purposes. The Central Bank's permission for the first loan was given on 21 January 2008 therefore it was not included in the regulatory capital as of 31 December 2007. The first loan matures on 19.12.2012 and the second loan matures on 20.12.2016. Each year in the last 5 years to maturity the amount of term debt recognized in Tier II capital is reduced by 20 percent.

In order to determine the capital requirements for credit and market risks the Bank Group distinguishes its positions into Trading and Banking portfolios (books). The Trading portfolio consists of positions in financial instruments and commodities held either with trading intent or in order to hedge other elements in the trading book. Such positions are held intentionally for short-term resale and/or with the intent to benefit from actual or expected short-term price movements or to lock in arbitrage profits. The Banking portfolio consists of balance and off-balance positions which do not classify as Trading book positions.

(3) *Capital requirements for credit risk*

DSK Bank Group applies the standardized approach for calculating its risk-weighted assets for credit risk. The local regulator sets out the risk weights which are applied on the positions from the Banking book based on the external credit assessment of each asset. The risk-weighted assets should consist of: (a) risk-weighted on-balance sheet assets, (b) risk-weighted off-balance sheet equivalents, (c) OTC derivative instruments weighted for counter party risk and (d) Trading portfolio positions weighted for counter party risk.

Directive 2006/48/EC of the European Parliament lays out the general framework of the standardized approach based on the risk scores from external credit assessment institutions for each exposure. It also allows applying of national discretions determined by the local regulator.

For risk weight calculation of rated exposures the Bank Group uses external credit assessments of the following credit agencies: Standard & Poor's; Moody's and Fitch Ratings with strict observation of the requirements of Chapter Four "Standardised Approach", Section Five "Additional Criteria for Use of ECAIs Credit Assessments" from Ordinance 8. ECAIs assessments are used for the next exposure classes: central governments or central banks, multilateral banks and institutions.

For the purposes of credit risk mitigation the Bank Group uses Financial Collateral Simple Method. During the process of credit risk mitigation for the purposes of Ordinance 8 capital calculation the Bank Group recognises collaterals as follow: financial collaterals – debt securities and cash on deposits; pledged insurance policies of Bulgaria Export Insurance Agency; guarantees; secured by first line mortgage residential property insured in favour of the Bank.

Since 2010 Bulgarian National Bank applies the Directive risk weight of 75 % for retail exposure portfolio and risk weight of 35 % for claims secured by residential property. The preferential treatment of 50 % risk weight for exposures secured by mortgages on commercial real estate is not allowed by the Authority.

The capital requirement for credit risk under the standardized approach is 12 %.

Exposures to credit and counterparty credit risk as at 31 December 2011

In thousands of BGN

Standardised Approach exposure class - On Balance sheet items	Original exposures before conversion factors		Impairment allowances	Breakdown of net exposure after impairment allowances by risk weights						Total net exposure after impairment allowances	Capital requirement
	before Credit Risk Mitigation	after Credit Risk Mitigation		0%	20%	35%	50%	75%	100%		
Central governments and central banks	628 739	690 888	-	656 476	-	-	34 412	-	-	690 888	2 065
Regional governments or local authorities	12 122	11 902	(311)	-	9 870	-	-	-	1 721	11 591	443
Administrative bodies and non-commercial undertakings	2 288	2 239	-	-	-	-	-	-	2 239	2 239	269
Multilateral development banks	8 088	8 088	-	8 088	-	-	-	-	-	8 088	-
Institutions	578 474	543 246	-	-	107 816	-	435 430	-	-	543 246	28 714
Corporates	1 335 650	1 316 245	(33 595)	-	-	-	-	-	1 282 650	1 282 650	153 918
Retail	2 811 265	2 793 677	(107 462)	-	-	-	-	2 686 215	-	2 686 215	241 759
Exposures secured by mortgages on residential property	2 286 059	2 285 767	(10 223)	-	-	1 821 525	-	-	454 019	2 275 544	130 986
Exposures in default	1 240 633	1 240 633	(888 884)	-	-	-	148 558	-	203 191	351 749	33 296
Collective investment units	391	391	-	-	-	-	-	-	391	391	47
Other exposures	562 217	572 850	(3 646)	176 406	70 793	-	-	-	322 005	569 204	40 340
Total	**9 465 926**	**9 465 926**	**(1 044 121)**	**840 970**	**188 479**	**1 821 525**	**618 400**	**2 686 215**	**2 266 216**	**8 421 805**	**631 837**

In thousands of BGN

Standardised Approach exposure class - Off Balance sheet items	Original exposures before conversion factors		Impairment allowances	Breakdown of net exposure after impairment allowances and before credit conversion by risk weights						Total net exposure after impairment allowances	Capital require-ment
	before Credit Risk Mitigation	after Credit Risk Mitigation		0%	20%	35%	50%	75%	100%		
Central governments and central banks	-	10 546	-	10 546	-	-	-	-	-	10 546	-
Regional governments or local authorities	2 193	2 193	-	-	2 193	-	-	-	-	2 193	7
Administrative bodies and non-commercial undertakings	839	-	-	-	-	-	-	-	-	-	-
Institutions	5 527	9 314	-	-	-	-	7 714	-	1 600	9 314	326
Corporates	426 759	404 913	-	-	-	-	-	-	404 913	404 913	12 993
Retail	150 259	137 188	-	-	-	-	-	137 188	-	137 188	671
Exposures secured by mortgages on residential property	69 295	69 230	-	-	-	30 554	-	-	38 676	69 230	1 271
Other exposures	3 442	24 930	-	18 970	2 576	-	-	-	3 384	24 930	27
Total	**658 314**	**658 314**	**-**	**29 516**	**4 769**	**30 554**	**7 714**	**137 188**	**448 573**	**658 314**	**15 295**

To measure the exposure to counterparty risk for over-the-counter derivatives DSK Bank Group assesses a capital charge based on the current market value (current exposure) of each contract and an estimate of additional credit exposure (referred to as the add-on for potential future exposure) that may arise as a result of fluctuations in prices or rates. The current exposure of a derivative contract is the market value of the contract if that value is positive, or zero if the market value is zero or negative. The add-on for potential future exposure is estimated by multiplying the notional principal amount of the contract by a credit conversion factor that is determined by the remaining maturity and type of contract – in the case exchange rate contracts with maturity of up to one year are assigned 1 %.

In thousands of BGN

Exposures to Counterparty Credit Risk - Standardised Approach exposure class	Original exposures before conversion factors		Impairment allowances	Breakdown of net exposure after impairment allowances by risk weights			Total net exposure after impairment allowances	Capital require-ment
	before Credit Risk Mitigation	after Credit Risk Mitigation		50%	75%	100%		
Institutions	868	868	-	651	-	217	868	65
Corporates	612	612	-	-	-	612	612	74
Retail	475	475	-	-	475	-	475	43
Total	**1 955**	**1 955**	**-**	**651**	**475**	**829**	**1 955**	**182**

(4) *Capital requirements for market risk*

Risk-weighted assets for position risk on the Trading book and risk-weighted assets for exchange rate risk on both the Trading and the Banking books compile the risk-weighted assets for market risk.

- *Capital requirements for position risk*

Capital requirements for both general and specific risk in each currency are calculated for the Bank Group's debt securities, equities and investments in collective investment units (CIU) which are in the Trading portfolio of the Group.

To calculate the capital requirements for general position risk of debt securities, the Bank Group uses maturity approach where the net position in each debt instrument is assigned a risk weight depending on its residual term to maturity. Fixed-rate instruments shall be assigned on the basis of residual maturity, and variable-rate instruments – on the basis of the period until the next interest rate change.

To calculate the capital requirements for specific risk of debt securities, the Bank Group assigns the net position in each debt instrument a risk weight related to the instrument issuer, its external credit assessment and its residual term to maturity.

Capital requirements for position risks as at 31 December 2011 - traded debt instruments

In thousands of BGN

Market risk: Standardised Approach for position risks in traded debt instruments	BGN	EUR	Risk weights	Capital requirements
General position risk. Maturity based approach				
0 ≤ 1 month	501	5 827	0.00%	-
> 1 ≤ 3 months	-	-	0.30%	-
> 3 ≤ 6 months	-	-	0.60%	-
> 6 ≤ 12 months	2 103	5 915	1.05%	84
> 1 ≤ 2 (1,9 for coupon of less than 3%) years	246	1 097	1.88%	25
> 2 ≤ 3 (> 1,9 ≤ 2,8 for coupon of less than 3%) years	8 680	-	2.63%	227
> 3 ≤ 4 (> 2,8 ≤ 3,6 for coupon of less than 3%) years	1 068	-	3.38%	36
> 4 ≤ 5 (> 3,6 ≤ 4,3 for coupon of less than 3%) years	-	10 673	4.13%	440
> 5 ≤ 7 (> 4,3 ≤ 5,7 for coupon of less than 3%) years	12 382	-	4.88%	604
> 7 ≤ 10 (> 5,7 ≤ 7,3 for coupon of less than 3%) years	27	-	5.63%	2
> 10 ≤ 15 (> 7,3 ≤ 9,3 for coupon of less than 3%) years	-	-	6.75%	-
Total	**25 007**	**23 512**		**1 418**
Specific position risk				
Debt instruments under first category (0% capital requirement)	25 007	23 512	0.00%	-
Total	**25 007**	**23 512**		-
Capital requirements for each currency	**895**	**523**		**1 418**

To calculate the capital requirements for general position risk, the group uses 12% risk weight assigned to the gross position in equities and 48% risk weight assigned to positions in CIU.

To calculate the capital requirements for specific risk of equities and CIU, a risk weight of 12% is assigned to the net position of the group.

Capital requirements for position risks as at 31 December 2011 - traded equities and CIU

Market risk: Standardised Approach for position risks in traded equities - national market	Net long position	Risk capital charges - %	Capital requirements
General position risk			
Equities - other	170	12.00%	20
Specific position risk			
Equities - other	170	12.00%	20
Positions in Collective investment units	1 440	48.00%	692
Capital requirements			**732**

- *Capital requirements for exchange rate risk*

A capital charge for exchange rate risk for the positions in both the Trading and the Banking book is applied only when the net open currency position exceeds 2% of the regulatory capital.

Since 1999 Bulgaria introduced a Currency Board and the local currency the Bulgarian lev had been pegged to the euro. Therefore the positions in euro are not included in the calculation of net open currency position nor are subject to capital requirement

Capital requirements for foreign exchange risk as at 31 December 2011

In thousands of BGN

Market risk Standardised Approach to foreign exchange risk	**All positions**		**Net positions**	**Capital requirement ***
	Long	**Short**		
Total positions in non-reporting currencies	**299 233**	**298 344**	**889**	**-**
Currencies in second stage of EMU	-	-	-	
All other currencies (including CIUs treated as different currencies)	299 233	298 344	889	
Currency positions				
EUR**	3 351 233	2 528 303	822 930	
GBP	19 104	19 037	67	
SEK	127	1	126	
CHF	4 349	4 481	(132)	
Other EEA currencies***	147	1	146	
USD	275 296	274 737	559	
CAD	198	87	111	
JPY	12	-	12	

* when Net positions exceed 2% of Total Own Funds for Solvency Purposes
** EUR positions are not included in Net Position nor is subject to capital requirements
*** RON и HUF

- *As of December 31, 2011the Bank Group doesn't calculate capital for settlement risk*

(5) *Capital requirements for operational risk*

DSK Bank Group applies the Basic Indicator Approach to calculate the capital requirement for operational risk. The Bank Group must hold capital for operational risk equal to the average over the three previous years of a fixed percentage (amounting to 15 %) of positive annual gross income. Gross income is defined as net interest income plus net non-interest income and gross of provisions for impairment losses and gross of operating expenses. The calculation should be based on audited financial data.

Capital requirements for operational risks as at 31 December 2011

In thousands of BGN

Banking activities	Gross income 2008	Gross income 2009	Gross income 2010	Capital requirement
Total banking activities subject to Basic Indicator Approach (BIA)	558 701	593 149	619 697	132 866

2. Internal Capital Adequacy Assessment Process (ICAAP)

DSK Bank identifies as specific for its profile the following types of risk:

- Credit risk
- Concentration risk
- Market risk
- Operational risk
- Interest rate risk in the Banking portfolio
- Liquidity risk
- Reputation risk
- Strategic risk

Risk management and control of the Bank have the following main goals:

- Achievement of the strategic goals of the Bank in a way which ensures the balance between assumed risks and realized earnings;
- The potential losses should be limited to an amount which the Bank is capable of bearing without endangering its long-term development.
- Risk management processes have to correspond to the applicable regulatory requirements and follow the best banking practices;
- DSK Bank follows a common and consistent risk management policy, which corresponds to the level of development of the Bank and is consistent with its size.

To guarantee the achievement of the main goals of the Bank, systems and processes for risk identification, measurement, monitoring, and reporting have been developed. The existent risks are subject to ongoing control in order to ensure they are limited to expected and acceptable amounts. The risk management bodies are responsible for preventive and ongoing risk management.

(1) Internal Strategy and Capital Plan

The determination of the required ratios and levels of capital is done as a part of the annual planning process of the Bank operations and revision of the long-term strategy. The internal management and analysis of the capital adequacy aims to maintain an adequate amount of internal capital which corresponds to the risk profile of the Bank and the respective systems for risk management. The following principles apply:

- A transparent corporate structure which ensures effective and rational risk management;
- Clearly defined levels of reporting and separation of tasks and responsibilities;
- Comprehensible and effective systems for risk control and internal control which are independent from the activities being controlled;
- Public announcement and transparency of the Bank operations;
- The Bank regulates the process of managing every type of material risk with separate rules.

The plans for development of the capital base are consistent with the goals for development of the Bank operations and the acceptable levels of risk according to these goals. So far, the short- and long-term goals of the Bank have always been set within its current risk profile without predicting significant changes in the levels of influence of the separate risk components. This allows a reliable assessment of the necessary development of the capital base and subsequent planning of an adequate capital position.

(2) Capital Management

The capital requirement is calculated according to the regulatory requirements, as well as according to the Internal Capital Adequacy Assessment Process. The regulatory requirements should be fulfilled with a reasonable reserve above the stipulated minimum. In case the ability to provide capital to cover the higher of the two requirements (including a reasonable reserve above the minimum capital requirement according to the regulatory requirements or the result reached by ICAAP) is under question, the Bank reviews its objectives and risk profile.

The Bank has sufficient capital to meet the regulatory requirements as well as a sufficient capital reserve to meet a more risk-sensitive environment.

In compliance with the policy of ICAAP, all future and current capital needs are determined in the context not only of the current business and economic conditions, but also of potential economic crises.

The main parameters of the internal system for capital assessment are the risk profile of the Bank, the risk components which structure this risk profile, the level of exposure of the different risk components, and the quality of management of the different risk components.

(3) Structure of the general capital resource of the Bank

Depending on the strategy for the profit of the Bank for the purposes of internal capital analysis, tier I capital could include the current year profits up to the moment at which, after the year end, the General Assembly will make a decision regarding its distribution, inclusion in tier I capital for regulatory purposes, or retention in undistributed profits from previous years.

The Bank has a stable and adequate capital position which allows coverage of the risks arising from its operations. The Bank foresees capital reserve for both the regulatory requirements for capital adequacy and for the necessary capital base obtained as a result of internal capital adequacy assessment. This capital reserve is a result mainly of the consistently followed policy for capitalization of profits from previous years. Due to this policy for profit capitalization, the Bank has also a stable enough position in tier I capital.

As the Bank (and the banking market in Bulgaria as well) does not have a long enough history operating with its specific risk profile in an economic environment with respective economic upsurges and declines, so that a reliable judgment regarding the degree of coverage can be drawn, for the purposes of the internal capital adequacy assessment, the Bank has set a more conservative level of the minimum capital requirement.

(4) *Additional capital according to ICAAP*

- Additional capital for credit risk

Despite of the availability and usage of up-to-date methods and models for credit risk assessment, the Bank recognizes that these models were developed in times of stable economic growth. Since the internal models have been employed since 2005, there is no experience in time of a recession, not to mention of a global economic crisis. For this reason the Bank believes that at the current moment it is not advisable to use elements of IRB approach for internal analysis of the capital adequacy as they may lead to underestimation of the capital coverage needs. As a consequence currently, the standardized approach is considered appropriate for calculation of the necessary capital according to ICAAP.

The management of the Bank believes that the risk profile of the portfolio is adequately covered by the allocated capital, as specified in the regulatory requirements. No need has been identified for additional capital coverage above the regulatory maximum.

- Additional capital for concentration risk

The Bank considers the level of its assets impairment high enough. In addition to the well defined limits regarding exposure concentration (industry limits, big exposures, customer limits) and the corresponding control and management rules and procedures it represents an additional reserve related to the risk from concentration. That is why the Bank considers that it is not necessary to allocate additional capital for concentration risk.

- Additional capital for currency risk

In accordance to the adopted internal Bank rules, the positions are monitored on a daily basis. In addition, a unit which is independent from the business calculates and reports the status and the total risk of the positions of the Bank. The level of foreign exchange risk is measured with a VaR model. The employed method is parametric and assigns higher weights to the last observations when deriving the correlational matrix. The model is constantly back-tested and the results are periodically reported to the management of the Bank.

The additional capital that the Bank provides based on calculations regarding currency risk levels is less than 0.01% of the Capital base.

- Additional capital for interest-rate risk in trading portfolio

The capital requirements for this type of risk are determined by the result obtained from a standard deviation (shock) of the interest rates in the different currencies. In the Rules for management of the interest rate risk of the Bank, a limit has been set regarding the effect of the standard shock. Taking into consideration the asset and liability structure, the management considers that the standard shock determines adequately the level of interest rate risk of the Bank and the result should be used for determining the required capital need which is about 2 % of the Capital Base.

- Additional capital for liquidity risk

The Bank considers that the capital is not an adequate tool for covering the liquidity risk.

- Additional capital for operational risk

Taking into account the damages from operating events which have been registered by the Bank and the recovered amount due to the existence of an effective system for loss control and limitation during the ICAAP process the Bank allocates 2 % from the Capital Base for capital needed for operational risk.

- Additional capital for reputation risk

Reputation risk can be broadly defined as a risk arising from any Bank operation or the activities of the Bank employees which can harm the Bank's image, reputation in the society, and the long-term confidence of clients, employees, and shareholders. This could lead to a decrease in sales and market share, deterioration of relationships with counterparties and clients, and a consequent deterioration of financial indicators.

As a result of reputation risk management and the calculated on that basis corrected ratio of sensitivity, the Bank calculates a total corrected ratio of sensitivity which is based on the different weights with which each risk could influence the total risk profile of the Bank. Given the assessment of the current levels of reputation risk, the Bank determined 0.27 % of its Tier I capital to cover the required additional capital for reputation risk.

- Additional capital for strategic risk

Strategic risk is the current or potential level of risk for the earnings and capital. This risk arises from a change in the business environment, unfavorable managerial decisions, incorrect execution of these decisions, or lack of a flexible response to the changes in the business environment. Strategic risk is the risk that under specific developments in the economic environment, the influence of different internal and external factors, or other risks, the Bank will not be able to achieve its strategic goals or will deviate significantly from them.

As a result of the strategic risk management and the observed historic deviation from the strategic goals, the Bank has set 0.33% of its Tier I capital as the required additional capital for covering the strategic risk.

II. Remuneration Policy and Practices

1. Remuneration Policy of the Bank Group

The taking decision process is in accordance with the Remuneration Policy Rules of the Bank and the Bank Group, developed and applied keeping the OTP Bank standards. The rules are accepted from the Management Board and approved from the Supervisory Board of DSK Bank.

The most important principle of the Bank Group Remuneration Policy is that the rate of performance-based remuneration – subject to the preliminary and subsequent evaluation of risks – is linked to realization level of the targets at bank group/bank and individual level.

The performance appraisal among the persons belonging to the scope of the Remuneration Policy is based on individual agreements. The performance expectations are defined by bank group/bank/affiliate, organizational, manager and position level within a pre-defined benchmark structure and/or target tasks considering the differences arising from the nature of the various banking organizations' activity.

The Remuneration Policy stipulates differentiated income levels conforming to the value of the jobs and based on classifications. The remuneration comprises fixed and performance-based remuneration. The fact that the amount of the fixed remuneration for the persons belonging to the scope of the Policy is high enough to provide compensation for the professional work and is in line with the level of education, ranking, the required level of experience and skills, and the relevant business sector ensures the enforcement of a flexible remuneration policy.

At the level of DSK Bank Group the performance appraisal connected to performance-based remuneration takes place on the basis of the return on risk-adjusted capital (RORAC). The ratio is calculated on the basis of the figures of those Bank Group member affiliates, operating as group members, which belonged to the circle of consolidation throughout the appraised fiscal year for controlling purposes.

As a general rule the performance remuneration based on performance appraisal for the persons belonging to the scope of the Remuneration Policy takes place uniformly in the form of cash bonus and shares, in the proportion of 50-50%.

As a general rule 60% of the performance-based remuneration specified for individual level for the persons belonging to the scope of the Remuneration Policy shall be deferred.

The main criteria for defining the personal scope of the Remuneration Policy are as follow:

- position, seniority within the corporate hierarchy;
- individual and collective decision-making authority linked to position;
- nature and complexity of the activity performed;
- degree and regularity of the supervision ensuring the performance of the pursued activity;
- business model of the business lines where he/she is active;
- respective market environment, labour market competitive position and local laws, and other local regulations.

The ratio of the fixed and performance-based remuneration connected to the various positions of additional persons belonging to the scope of the Remuneration Policy is established, based on the subject to the collective consideration of the aspects below:

- performance appraisal system and method of defining the risk levels;
- length of the deferred appraisal and payment period, and of the retention period;
- the structure of the organizational unit / Bank Group member affiliate, nature and complexity of its activity;
- position of the employees within the organizational hierarchy, and risk assumption/decision-making levels allocated to the various positions.

2. *Total remuneration broken down by business area of the Bank is as follow:*

In thousands of BGN

Retail banking	30 365
Corporate banking	3 454
Risk management	4 969
IT	4 460
Support and Service	17 324
Subsidiaries	7 038
Total	**67 610**

3. *Aggregate quantitative information on remuneration of the persons referred to in Article 2, items 1, 2 and 4 of BNB Ordinance No. 4 of 2010 on the Requirements on the Remuneration in Banks:*

- the amount of remuneration for the financial year split into fixed and variable remuneration, and the number of beneficiaries:

  Fixed annual remuneration - 6 143 thousands of BGN / 98 persons;
  Variable annual remuneration - 3 539 thousands of BGN / 98 persons.

- the amount and form of variable remuneration is 3 539 thousands of BGN – cash;
- the amount of outstanding deferred remuneration that are to be paid till 2015 is 1 244 thousands of BGN;
- there is no amount of deferred remuneration awarder during the financial year paid out and reduced through performance adjustments;
- new sign-on and severance payment made during the financial year, and the number of beneficiaries of such payments is 45 thousands of BGN to one payee;
- the amount of severance payments awarded during the financial year and the number of beneficiaries is 45 thousands of BGN to one payee.

Violina Marinova
Chief Executive Director

Dorothea Nikolova
Executive Director