



ANNUAL FINANCIAL REPORT

2017

CAFFIL

Public sector assets – *Obligations foncières*
to support the French economy.

ANNUAL FINANCIAL REPORT 2017

Caisse Française de Financement Local

CAFFIL

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This free translation of the annual financial report published in French is provided solely for the convenience of English-speaking readers.

Profile

Caisse Française de Financement Local (also known by its acronym CAFFIL) is an issuer of covered bonds with a portfolio of assets solely comprised of loans to public sector entities. It is fully owned by the French State-owned development bank SFIL.

Caisse Française de Financement Local is a French specialized credit institution (*société de crédit foncier*). Its sole business is the refinancing of loans to public sector entities through the issue of covered bonds, called *obligations foncières*.

Caisse Française de Financement Local and its parent company have been tasked by the French State:

- to finance loans to French local governments and public hospitals granted by La Banque Postale;
- to refinance large export credits with the unconditional and irrevocable guarantee of the French State.

Caisse Française de Financement Local is a wholly-owned subsidiary of SFIL, which also manages the Company in accordance with article L.513-15 of the Monetary and Financial Code. SFIL is a credit institution approved by the Autorité de contrôle prudentiel et de résolution (ACPR), 75% of which is held by the French State, its reference shareholder, 20% by Caisse des Dépôts et Consignations (CDC) and 5% by La Banque Postale (LBP). The shareholding structure of Caisse Française de Financement Local is thus firmly anchored in the public sphere, reflecting the missions entrusted to it by the French State.

CAFFIL is the leading European issuer of covered bonds, which are secured by a portfolio of public sector loans. The Company issues *obligations foncières* (covered bonds) regularly. Their primary characteristics are that:

- they are regulated by specific legal provisions;
- they are rated AA+/Aaa/AA by Standard and Poor's, Moody's, and Fitch;
- they comply with the EU's UCITS and CRD directives, and with article 129 of the CRR standard;
- they benefit from the Covered Bond Label created by the European Covered Bond Council (ECBC).

The *obligations foncières* issued by CAFFIL are thus eligible for refinancing by the European Central Bank (ECB) and thus enable investors to benefit from the best prudential treatment.

In 2016, CAFFIL was named the best issuer of the year for its covered bonds in euros by three separate specialized publications (*The Covered Bond Report* in June, *The Cover* in September, and *CMD Portal* in December). In 2017, for the second consecutive year, CAFFIL was named the best issuer of the year by *CMD Portal*.

Key figures

as of December 31, 2017

Portfolio of assets
(cover pool)

EUR 55.8 billion

Assets eligible for the central bank
(% cover pool)

75.3%

Non-performing and litigious loans
(% cover pool)

1.0%

Common Equity Tier 1 Ratio
(Basel III – fully loaded)

23.2%

Obligations foncières
(covered bonds)

EUR 49.0 billion

Obligations foncières issued
in 2017

EUR 6.0 billion

Regulatory
over-collateralization

111.6%

Liquidity Coverage Ratio
(LCR)

371%

Management Report

Caisse Française de Financement Local

2017

1. General presentation of Caisse Française de Financement Local

1.1 - NATURE AND ACTIVITIES OF THE COMPANY

Caisse Française de Financement Local (also known by its acronym CAFFIL) is a credit institution active in the refinancing of loans to public sector entities through the issue of covered bonds, which are called *obligations foncières*.

It is a specialized credit institution authorized to operate as a *société de crédit foncier*. As a credit institution, the Company is subject to all legal and regulatory provisions that apply to credit institutions. It conducts banking transactions in its ordinary course of business. As a *société de crédit foncier*, it engages in transactions that are specialized and have an exclusive purpose, as defined in articles L.513-2 and following of the Monetary and Financial Code.

In the case of Caisse Française de Financement Local, this specialization is exclusively limited to transactions with public sector entities or entities they guarantee as specified in its October 1, 1999, authorization and its own by-laws:

- The authorization mentions that the Company “is approved as a *société de crédit foncier*, the activities of which exclusively concern the granting or acquisition of loans to public sector entities or those they guarantee, as well as the holding of securitization units or shares of similar entities when the assets in these securitizations are for at least 90% composed of assets of the same nature as the above-mentioned loans, in accordance with article 94-II and III of law 99-532”.
- The purpose of the Company (article 2 of the by-laws) specifies that the exclusive purpose of the Company is:
 - to grant or to acquire exposures on public sector entities as defined in article L.513-4 of the Monetary and Financial Code as well as securitization units or shares of similar entities considered as exposures on public sector entities as defined in article L.513-5 of the Monetary and Financial Code;
 - to hold securities and other assets under the conditions set by decree to be considered as replacement assets.

Sociétés de crédit foncier, which were created by the law of June 1999, are now well-known in the world of bond issuers and investors. They issue covered bonds called *obligations foncières* and contract other covered debt negotiable or not in regulated markets. All these instruments are characterized by the legal privilege that primarily affects cash flows from the Company's assets to pay the interest and reimbursement of the *obligations foncières*. *Sociétés de crédit foncier* may also issue or contract non-covered debt. *Obligations foncières* constitute a significant element in the international covered bond market.

1.2 - LEGAL AND SHAREHOLDING STRUCTURE OF THE COMPANY

1.2.1. Legal structure and name of the Company

The Company was created on December 29, 1998, for a period of 99 years. It was authorized to operate as a *société de crédit foncier* by the Comité des établissements de crédit et des entreprises d'investissement (now a part of ACPR) at its meeting on July 23, 1999. The authorization became definitive as of October 1, 1999.

On January 31, 2013, the Company took the name Caisse Française de Financement Local to replace that of Dexia Municipal Agency, upon the sale of its sole shareholder, Société de Financement Local (renamed SFIL in June 2015), to the French State, Caisse des dépôts et consignations and La Banque Postale.

The Company's registered office is located at 1-3, rue du Passeur de Boulogne in Issy-les-Moulineaux (92130), France.

Caisse Française de Financement Local is a *société anonyme à directoire et conseil de surveillance*, a joint-stock corporation with an Executive Board and a Supervisory Board, under the provisions of articles L.210-1 and following of the Code of Commerce. Its operation is regulated by articles L.511-1 and following (credit institutions) and L.513-2 and following (*sociétés de crédit foncier*) of the Monetary and Financial Code.

1.2.2. Shareholding structure of the Company

Caisse Française de Financement Local and its parent company SFIL are key elements in the financing of local governments and public hospitals in France. The organization, introduced by the French State in 2013, is based on a commercial activity developed by La Banque Postale with refinancing provided by Caisse Française de Financement Local. Since 2015, the French State has entrusted SFIL and Caisse Française de Financement Local with a second mission that is the responsibility to refinance large export credits with the guarantee of the State (see 1.3.2.). The objective is to enable

large export credits, as well as French local governments and public hospitals to benefit from optimal financing conditions through a high rating and irreproachable risk management.

The capital of Caisse Française de Financement Local is 100% held by SFIL, which also manages the Company in accordance with article L.513-15 of the Monetary and Financial Code. SFIL is a credit institution approved by the Autorité de contrôle prudentiel et de résolution (ACPR). Its shareholders are the French State (75%), Caisse des dépôts et consignations (20%) and La Banque Postale (5%). SFIL's shareholders are thus firmly anchored in the public sphere, reflecting the missions the French State assigned it.

The French State is the "reference shareholder" of SFIL and Caisse Française de Financement Local for ACPR, underlining its commitment to ensure oversight and to influence strategic decisions, as well as its determination to ensure Caisse Française de Financement Local's and SFIL's ongoing financial transactions and to comply with regulatory requirements, if so required.

1.3 – ECONOMIC MODEL OF CAISSE FRANÇAISE DE FINANCEMENT LOCAL

1.3.1. Refinancing of loans to the French local public sector and public hospitals in partnership with La Banque Postale

In early 2013, Caisse Française de Financement Local and La Banque Postale signed an exclusive sale agreement to fund the needs of the French local public sector and public hospitals. The arrangement, set up under the aegis of the French State, works as follows: La Banque Postale markets loans to the French local public sector and public hospitals, then sells them to Caisse Française de Financement Local, which refinances them by issuing *obligations foncières* (covered bonds). The loans originated are exclusively in euros with a vanilla interest rate. La Banque Postale committed to propose to Caisse Française de Financement Local all the loans that would be eligible for its cover pool.

This partnership enables Caisse Française de Financement Local to maintain its control of the credit risk through a two-stage analysis.

- When the loan is originated, the initial analysis of the counterparty is carried out simultaneously at the two entities. The loans that do not meet the credit and eligibility criteria of Caisse Française de Financement Local cannot be transferred to its balance sheet. Caisse Française de Financement Local's eligibility criteria are strictly monitored by internal management policies and limit eligible counterparties to French local public sector entities and public hospitals.
- Before loans originated by La Banque Postale are sold to Caisse Française de Financement Local, a new analysis of the assets is conducted, and Caisse Française de Financement Local may refuse a loan prior to the sale if the asset no longer meets the criteria.

As required by law, the sale of loans to Caisse Française de Financement Local is carried out by using a transfer form (*bordereau de cession*) that is specific to *sociétés de crédit foncier*.

1.3.2. Refinancing of large export credits

In addition to their mission of refinancing French local governments and public hospitals, SFIL and Caisse Française de Financement Local have been entrusted with a second mission by the French State: to refinance large French export contracts, with the objective to support French exports in terms of financial competitiveness, in accordance with a public refinancing plan comparable to that of other OECD countries. In this context, SFIL signed a protocol agreement governing relations with 20 commercial banks, thereby confirming relations with almost all the banks active in the French export credit market. SFIL may acquire all or a part of the participation of each of these banks in an export credit.

In this context, Caisse Française de Financement Local grants loans to SFIL in order to refinance its export credits. Such loans benefit from an irrevocable and unconditional 100% guarantee by the French State (enhanced guarantee⁽¹⁾). This business brings Caisse Française de Financement Local closer to the French State, without modifying the risk profile of its cover pool.

These new loans, like the new French public sector loans marketed by La Banque Postale, are added to the portfolio of Caisse Française de Financement Local, which is financed by the issue of *obligations foncières*. Given the current size of the cover pool and the growth of its traditional line of business, the percentage share of this new activity will increase gradually and will only become significant in several years. This share may rise to 13% until 2021, based on an annual production of large export credits of more than EUR 2.0 billion.

1.3.2.1. Organization

The system functions as follows:

- SFIL contributes to the financial proposal made by one or more banks in the banking syndicate granting the buyer credit covered by the export credit insurance guaranteed by the French State.
- After the export contract finalization, these banks sell a part of the loans (and the attached rights) to SFIL and keep at least the share of the export credit not covered by the insurance (usually 5%).
- Caisse Française de Financement Local grants a loan to SFIL to enable it to refinance the acquired export credit. This refinancing loan benefits from an irrevocable and unconditional 100% guarantee by the French State, referred to as an enhanced guarantee.

(1) The enhanced guarantee was introduced by law 2012-1510 of December 29, 2012, and the decree 2013-693 of July 30, 2013.

Loans granted by Caisse Française de Financement Local to SFIL to refinance the purchased export credits thus constitute exposures that are totally guaranteed by the French State and eligible for the cover pool of a *société de crédit foncier*. These loans also comply with the European CRR regulation (article 129, which specifies the assets authorized for inclusion in a cover pool to ensure that the covered bonds will benefit from the best prudential treatment).

1.3.2.2. French State export guarantees

Previously granted by Coface, since late 2016, these guarantees have been managed by Bpifrance Assurance Export, in the name of, on behalf of, and under the control of the French State, pursuant to article L.432.2 of the Insurance Code.

- Guarantee-granting decisions are made by the Minister in charge of the Economy and Finances after instruction by Bpifrance Assurance Export and the opinion of the French Export Credit and Guarantee Commission (*Commission des garanties et du crédit au commerce extérieur*).
- Bpifrance Assurance Export issues insurance policies, as well as enhanced guarantees, in accordance with the decision made. In this context, Bpifrance Assurance Export is also tasked with collecting insurance and guarantee premiums, managing risks, payments, and collections on behalf of the French State.
- The risks related to these guarantees are borne by the French State and all financial flows (premiums, payments, repayments) are recorded in separate accounting entries by Bpifrance Assurance Export. Premiums and collections are received directly on the account of the French State, and payments are made directly from the same account, without passing through the accounts of Bpifrance Assurance Export.

1.3.3. Servicing and financing provided by SFIL

The role of SFIL primarily involves the following:

- to ensure the complete operational management of the Company (day-to-day management as well as the operational management of the reduction in the sensitivity of the structured loans on the balance sheet of Caisse Française de Financement Local), as defined by the regulations applicable to *sociétés de crédit foncier*, in particular article L.513-15 of the Monetary and Financial Code;
- to provide Caisse Française de Financement Local with some of the derivatives and non-privileged funding it needs to carry out its activities.

The funds required to finance the activity of Caisse Française de Financement Local (financing of over-collateralization and intermediated derivatives) are obtained by SFIL:

- either by its shareholders under credit agreements:
 - Caisse des dépôts et consignations (CDC) for all the needs linked to operations booked prior to the date of acquisition of SFIL (January 31, 2013) and to the new export refinancing activity;
 - La Banque Postale (LBP) for all the needs related to loans to French local public sector and public hospitals that it originates.
- or on financial markets by issuing short-term debt (certificates of deposit) or long-term debt (bonds), in order to diversify its financing sources. In the French State Agencies segment, SFIL gradually set up its signature by launching a first benchmark issue in the last quarter of 2016, followed by two new benchmark issues, including one in USD, in 2017.

In addition to commitments of the French State as the reference shareholder, on January 31, 2013, SFIL signed a declaration of support of Caisse Française de Financement Local, which is reproduced in this annual financial report – General information.

It should be noted that SFIL also supplies services for the business of lending to French public sector entities engaged by La Banque Postale (LBP) and its joint venture LBP/CDC, La Banque Postale Collectivités Locales. These services concern activities involving commercial support, financial oversight, the supply of data for risk analysis and back office operations.

1.3.4. Other management agreements

Specific individual agreements have been established with entities that, in the past, have transferred assets to the *société de crédit foncier*, and continue to ensure management for their national clientele. These assets are now managed in a run-off mode. At the end of 2017, there were agreements with the following entities: Kommunalkredit Austria (Austria), Belfius Banque et Assurances (Belgium), and Dexia Crediop (Italy). These agreements already existed in previous years.

Starting in 2015, management of new registered covered bonds (RCB) is entrusted to Landesbank Baden-Württemberg (LBBW). Dexia Kommunalbank Deutschland continues to manage registered covered bonds issued prior to 2015.

1.4 - LEGAL FRAMEWORK

1.4.1. European framework

The *obligations foncières* issued by Caisse Française de Financement Local are covered bonds. Many countries have passed specific legal provisions for covered bonds in recent years, and the number of issuers has risen significantly.

Two directives govern and define covered bonds:

- The first directive is Undertakings for Collective Investment in Transferable Securities (UCITS) on the legislative, regulatory, and administrative aspects of certain vehicles for collective investment in securities, article 52-4.

- The second is the Capital Requirements Directive (CRD), on the minimum regulatory capital requirement, which is complemented by the related Capital Requirements Regulation (CRR), article 129.

These two directives in particular specify the assets that may be incorporated into the portfolio financed by the covered bonds, the privilege that protects investors, as well as the required level of public oversight and transparency in terms of communication. Investors in bonds that satisfy the requirements of these two directives and the associated regulation benefit from financial and regulatory advantages.

The *obligations foncières* issued by Caisse Française de Financement Local satisfy the requirements of these two European directives and the associated regulation. In this regard, they benefit from a 10% preferential risk weighting in the calculation of the solvency ratio with the standard method (given their current rating). Current and future *obligations foncières* issued by Caisse Française de Financement Local respect the conditions of eligibility for refinancing by the European Central Bank.

In addition, all the *obligations foncières* backed by the cover pool of Caisse Française de Financement Local benefit from the Covered Bond Label, which was created in 2012 by the European Covered Bond Council (ECBC) to improve the quality of financial information and the transparency of the European covered bond market.

To meet Label requirements, Caisse Française de Financement Local committed to respect the above-mentioned directives and to ensure a high level of transparency in its communication to investors. All detailed information on the issues and cover pool of Caisse Française de Financement Local is now posted on the Covered Bond Label site (<https://www.coveredbondlabel.com/issuer/47/>). It includes the harmonized transparency template (HTT) reporting used by all beneficiaries of the label. Since the end of 2015, the European Banking Authority and the European Commission have been leading a project to harmonize the legal framework of European covered bonds, which in 2017 was the subject of numerous discussions among the various stakeholders. The European Commission published a draft package (directive and regulation) on March 12, 2018, with an implementation target of mid-2019.

1.4.2. French legislative framework and regulations

Sociétés de crédit foncier are governed by the contents of articles L.513-2 to L.513-27 and R.513-1 to R.513-18 of the Monetary and Financial Code.

These articles of the law are complemented by the following regulatory texts:

- regulation 99-10 of the Comité de la réglementation bancaire et financière of July 9, 1999, as amended, relating to *sociétés de crédit foncier* and *sociétés de financement de l'habitat*;
- ACPR instructions 2011-I-06, 2011-I-07, 2014-I-16 and 2014-I-17.

In addition to these regulations and the law on *sociétés de crédit foncier*, which is described below, Caisse Française de Financement Local is subject to the same obligations as credit institutions in terms of reporting vis-à-vis the regulator and respect for liquidity ratios. The solvency ratio, large exposures and the leverage ratio are reported to the regulator on a consolidated basis, at the level of the parent company SFIL.

1.4.2.1. General framework

Article L.513-2 describes the general framework of the activities of *sociétés de crédit foncier*, in particular:

- their exclusive purpose which is to finance guaranteed home loans or loans to the public sector, or replacement assets, and the issue of *obligations foncières* and other resources benefiting or not from the legal privilege;
- the possibility to obtain financing by assigning in guarantee certain assets (which no longer contribute to the calculation of over-collateralization);
- the impossibility of owning subsidiaries or affiliates.

Application to Caisse Française de Financement Local

The assets are comprised of commitments on public sector entities. These assets are financed through the issue of debt that is covered by a legal privilege that guarantees them a priority right on the cash flows generated by the assets. The portion of assets that is not financed by covered debt – over-collateralization – is funded by the Company's equity and debt that does not benefit from the privilege, which is subordinated to the covered debt. Non-privileged debt is provided by SFIL, the sole shareholder of Caisse Française de Financement Local.

Since Caisse Française de Financement Local is not allowed to have any subsidiaries or affiliates, it does not publish consolidated financial statements and has no obligation to produce IFRS financial statements. Nonetheless, for reasons of comparability and transparency, Caisse Française de Financement Local publishes annual and half year financial statements according to IFRS.

1.4.2.2. Assets

Articles L.513-3 (home loans), L.513-4 (commitments on public sector entities), L.513-5 (securitization units) and L.513-6 (replacement assets) define the exposures that may be included in the assets of *sociétés de crédit foncier*.

Application to Caisse Française de Financement Local

The assets held by Caisse Française de Financement Local are solely comprised of commitments on public sector entities that are eligible by the terms of article L.513-4 of the Monetary and Financial Code, i.e. States, local governments or groups of such, public sector entities in the European Economic Area, Switzerland, the United States of America, Canada and Japan. These commitments are comprised of loans and bond issues representing a commitment on, or totally guaranteed by, these public bodies. Exposures to foreign public sector entities were marketed by the company's former shareholder

and are now managed in a run-off mode. Since 2013, all of Caisse Française de Financement Local's new assets relate to French borrowers.

Other assets, which current legislation calls replacement assets, may be acquired if they correspond to exposures on credit institutions benefiting from at least a Step 1 rating (level triple A or double A) or, when their maturity does not exceed 100 days, from a Step 2 rating (level simple A), their total amount is limited to 15% of the total of outstanding *obligations foncières* and other debt benefiting from the legal privilege (registered covered bonds in the case of Caisse Française de Financement Local). This asset category is used for cash investments by the Caisse Française de Financement Local.

1.4.2.3. Liabilities and the privilege

Article L.513-2 specifies that to finance their assets, *sociétés de crédit foncier* may issue debt that benefits (*obligations foncières* or other covered resources) or does not benefit from the privilege. Article L.513-10 makes it possible to hedge the assets and the privileged liabilities by derivative instruments that thus benefit from the privilege.

Article L.513-15 requires that a *société de crédit foncier* entrust the management of its operations to another credit institution with which it has signed an agreement. To maintain the privilege that benefits investors in *obligations foncières* and other covered resources, a *société de crédit foncier* should not have any employee (who would benefit in French law from a first-rank privilege). This management agreement itself benefits from the privilege of article L.513-11, *pari passu* with holders of privileged debt.

Article L.513-11 describes this privilege, in particular:

- that when a *société de crédit foncier* is subject to bankruptcy or liquidation procedures, cash flows generated by the assets, after any financial instrument hedges if such be the case, are allocated in priority to serve the *obligations foncières* and other resources benefiting from the privilege, also after any financial instrument hedges if such be the case;
- that the liquidation of a *société de crédit foncier* does not accelerate the reimbursement of *obligations foncières* and other debt benefiting from the privilege, which continue to be paid at their contractual due dates with priority over all other commitments. These other commitments can only be settled after all debt benefiting from the privilege has been discharged.

Article L.513-20 stipulates that the bankruptcy or liquidation of the shareholder of a *société de crédit foncier* cannot be extended to the *société de crédit foncier*.

Lastly, article L.613-55-1.I of the Monetary and Financial Code, transposing the BRRD, stipulates that *obligations foncières* cannot be used to absorb losses in the event of the resolution of a *société de crédit foncier* (bail-in).

Application to Caisse Française de Financement Local

The contracts of Caisse Française de Financement Local that benefit from the legal privilege are the *obligations foncières* and registered covered bonds that it issues, the hedging derivative contracts and the servicing agreement signed with SFIL. In addition to its equity, Caisse Française de Financement Local uses two categories of debt to finance its assets:

- debt that benefits from the legal privilege, defined by law as *obligations foncières* or other resources benefiting from the legal privilege by reason of their contract. Caisse Française de Financement Local thus issues registered covered bonds benefiting from the legal privilege by reason of their contract in the same way as *obligations foncières*; intended for German institutional investors, these private placements governed by German law also benefit from the French legal privilege attached to issues of *sociétés de crédit foncier*;
- debt that does not benefit from the legal privilege includes debt that is not covered by the assets and which, for this reason, is subordinated vis-à-vis debt benefiting from the privilege (see 5. Debt benefiting from the legal privilege). With equity, it finances over-collateralization. It may be of three types:
 - debt negotiated according to the terms of a financing agreement signed with the parent company;
 - refinancing in its own name from the Banque de France. Caisse Française de Financement Local implemented the organizational and IT procedures required to participate in the refinancing operations of the Banque de France, and tests them regularly. The financing obtained does not benefit from the privilege specified by the legislation on *sociétés de crédit foncier*, but is guaranteed by assets assigned to the central bank. These pledged assets are temporarily excluded from the cover pool and the calculation of the over-collateralization ratio;
 - financing obtained from credit institutions within the framework of repurchase agreements (repo).

In addition, on January 31, 2013, SFIL, the parent company of Caisse Française de Financement Local, signed a declaration of support ensuring that "Société de Financement Local and the French State, its reference shareholder, will ensure that Caisse Française de Financement Local will always be able to pursue its activity in an ongoing manner and to honor its financial commitments in compliance with the obligations imposed by banking regulations in effect". This declaration of support is reproduced in issuance documents and the annual financial report of Caisse Française de Financement Local.

1.4.2.4. Other provisions

The other articles of the Monetary and Financial Code define management and control procedures for *sociétés de crédit foncier*. They can be consulted on the Company's Website (<http://www.caffil.fr/en/portrait/la-loi/>) or on the official Legifrance Website (<http://www.legifrance.gouv.fr/>).

It can be noted that article L.513-12 and article R.513-8 of the Monetary and Financial Code require that the over-collateralization ratio, i.e. the ratio between the assets covering the privileged debt and the debt benefiting from the privilege at all times be greater than 105%.

The items concerning this ratio, as well as the management of the interest rate, foreign exchange and liquidity risks are discussed below in the chapters dedicated to these subjects.

1.5 - RATINGS OF THE *OBLIGATIONS FONCIÈRES* ISSUED BY CAISSE FRANÇAISE DE FINANCEMENT LOCAL

The issuance program of Caisse Française de Financement Local is rated by three of the main rating agencies – Standard & Poor's (S&P), Moody's and Fitch.

The ratings of the bonds issued by Caisse Française de Financement Local are at the highest level of credit quality (Step 1). This requires that the quality of the cover pool and strict management rules be consistent with the criteria and approaches of the three agencies.

The principle by which each agency rates *obligations foncières* (and covered bonds in general) involves taking as a starting point the issuer's rating or that of the parent company if the issuer is not rated, and enhancing this rating by one or more notches in function of the current safeguards (legal framework, quality of assets, asset/liability management, over-collateralization, etc.).

The rating of SFIL is now set at the same level as that of France for S&P and one notch below France for Moody's and Fitch. These very good ratings have been attributed because the agencies consider SFIL as an entity that is linked to the French government. They take into account a strong probability that the French State will provide extraordinary support to SFIL if necessary because of the strategic importance of the public service responsibilities SFIL was entrusted with, State commitments and the State's influence on SFIL's governance.

The close relationship between Caisse Française de Financement Local and the French State, due to its shareholding structure and support, but also to its mostly French cover pool, creates a link between the rating of *obligations foncières* and the rating of France for Fitch. Fitch's rating may thus not be higher than the sovereign rating; otherwise Fitch would apply an ultra-stressed rating scenario (an 80% default rate, with recoveries limited to 20%), making it necessary to have a level of over-collateralization that would be incompatible with the profitability of the business model.

Besides, the rating of *obligations foncières* is limited by S&P to one notch above the rating of SFIL and consequently to one notch above the rating of the French State, by reason of the non-conformity of certain derivative contracts with the agency's most recent methodological criteria (counterparties not rated by S&P or absence of a replacement clause).

Lastly, since the end of 2017, the *obligations foncières* issued by Caisse Française de Financement Local benefit from a Prime rating from the extra-financial rating agency Oekom by reason of the Company's performance in societal and environmental issues.

2. Highlights of 2017

2.1 - THE COVERED BOND MARKET

The primary market for public euro-denominated covered bond issues (benchmark public issues) was active in 2017, but its volume fell compared with previous years: EUR 115 billion, compared with EUR 127 billion in 2016 and EUR 146 billion in 2015. This decrease stemmed mainly from Canadian issuers, who focused on more favorable non-euro issues, as well as Spanish issuers, who instead used the long-term financing operations (TLTRO) available from the ECB on favorable terms.

Business nevertheless remained buoyant in 2017. The high issuance volumes are mainly attributable to the significant refinancing of bonds that matured in 2017 (EUR 123 billion), but also to the significant growth in Dutch issuance (8% of supply) and the active presence of non-eurozone issuers for whom this market's long-term financing conditions were favorable. German and French issuers remained the most active, accounting for more than 39% of supply, while Norwegian, Australian and UK issuers combined accounted for 15% of the market (no change from 2016).

During the first half of 2017, elections in Europe (Netherlands, France and Germany) affected the value of these countries' covered bonds. Nevertheless, despite a period of consolidation in the first half of the year, these events did not affect the solidity of the euro covered bond market, which performed robustly over the year as a whole.

In 2017, the market continued to benefit from the strong support provided by the ECB's covered bond purchase program, which totaled nearly EUR 241 billion as of December 31, up by around EUR 37 billion from a year earlier.

In this context, Caisse Française de Financement Local implemented its annual covered bonds financing program with good conditions of volumes, spreads and average maturities (EUR 6.0 billion issued, with an average maturity of more than 11 years). This allowed it to provide the long-term liquidity needed to refinance La Banque Postale's commercial offer for the French public sector, to develop a large export credit refinancing activity and to support the sensitivity reduction policy.

In 2018, in a changing regulatory environment (Basel III and Solvency 2), we expect the very favorable treatment enjoyed by covered bonds to encourage investors to prioritize them in their asset allocation. Demand should also be naturally supported by the maturing of significant volumes (around EUR 90 billion) of covered bonds; it is estimated that net supply in 2018 will be zero or slightly positive (versus negative net supply of EUR 8 billion in 2017).

2.2 - RATING OF OBLIGATIONS FONCIÈRES

The ratings of the *obligations foncières* issued by Caisse Française de Financement Local were not altered in 2017.

As of December 31, 2017, the ratings were as follows: AA+ by Standard and Poor's, Aaa by Moody's and AA by Fitch. The outlook associated with each of these ratings is stable.

2.3 - REFINANCING OF PUBLIC SECTOR LOANS GRANTED BY LA BANQUE POSTALE

In its first line of business, Caisse Française de Financement Local refinances loans granted by LBP to French local governments and public hospitals.

In this context, in 2017, Caisse Française de Financement Local acquired a total of EUR 3.3 billion in loans, which is roughly 14% more than the volume acquired from La Banque Postale in 2016 (EUR 2.9 billion). Since the beginning of the partnership, loans acquired through LBP have accounted for almost EUR 12.2 billion.

Since 2015, the CAFFIL/SFIL/LBP network has been recognized as the largest provider of funding for the French local public sector.

2.4 - LARGE EXPORT CREDITS REFINANCING

In its second line of business, Caisse Française de Financement Local grants loans to SFIL to refinance large export credits it has granted. Such loans benefit from an unconditional and irrevocable 100% guarantee by the French State. This new business brings Caisse Française de Financement Local closer to the French State without modifying the risk profile of its cover pool.

After a first year launching the business in 2016, in 2017 Caisse Française de Financement Local granted SFIL refinancing loans for a total amount of EUR 2.6 billion, compared to EUR 0.6 billion the previous year. The drawing of these loans is staggered over a number of years.

2.5 - SENSITIVITY REDUCTION AND DECREASE IN LITIGATION RELATED TO STRUCTURED LOANS

Caisse Française de Financement Local has, in its portfolio, some structured loans considered as sensitive (see 4.2.4.) which had been granted to French clients by Dexia Credit Local before the acquisition of Caisse Française de Financement Local by SFIL. Certain of these customers initiated legal proceedings against Dexia Credit Local, Caisse Française de Financement Local and/or SFIL.

The structured loan sensitivity reduction policy implemented by SFIL since its creation in early 2013 has made it possible to effect a significant reduction in both the size of Caisse Française de Financement Local's sensitive structured loan portfolio (see 4.2.4.) and the number of lawsuits (see 9.2.5.). This trend continued in 2017.

3. Changes in main balance sheet items

EUR billions value after currency swaps	12/31/2015	12/31/2016	12/31/2017	Change Dec. 2017 / Dec. 2016
Cover pool	60.0	58.2	55.8	(4.2)%
Loans	50.5	47.0	46.9	(0.2)%
Securities	7.0	7.5	7.2	(4.4)%
Cash deposit in central bank	2.5	3.7	1.7	(53.7)%
Privileged debt	53.0	51.7	49.7	(3.7)%
Obligations foncières ⁽¹⁾	51.6	50.4	49.0	(2.6)%
Cash collateral received	1.4	1.3	0.7	(45.6)%
Non-privileged debt	5.5	5.2	4.8	(7.6)%
SFIL	5.5	5.2	4.8	(7.6)%
Equity IFRS (excluding gains and losses through equity)	1.5	1.4	1.5	2.9%

(1) Including registered covered bonds

As of December 31, 2017, Caisse Française de Financement Local's cover pool excluding accrued interest not yet due amounted to EUR 55.8 billion, reflecting a 4.1%, or EUR 2.4 billion decrease from its end-2016 level of EUR 58.2 billion. Caisse Française de Financement Local's cover pool is composed of loans and debt securities and also includes the temporary cash surplus put aside to anticipate the forthcoming repayment of *obligations foncières* or the refinancing of new export loans. This cash is deposited at the Banque de France, or invested in bank or European public sector securities. The cash surplus, placed with the Banque de France, represents EUR 1.7 billion at the end of December 2017, versus EUR 3.7 billion at the end of December 2016. The cash surplus invested in securities or lent to SFIL represents a total of EUR 1.6 billion as of December 31, 2017 versus EUR 0.9 billion at the end of December 2016.

As of December 31, 2017, no assets were excluded from the cover pool in order to be sold to a bank in a repurchase agreement or assigned in guarantee to the Banque de France.

As of this date, outstanding debt benefiting from the legal privilege, including cash collateral received, was EUR 49.7 billion, which decreased 3.7% in comparison with December 2016.

As of December 31, 2017, the debt contracted with the parent company totaled EUR 4.8 billion and does not benefit from the legal privilege. It mainly corresponds to the financing of the over-collateralization of the cover pool which is at a significantly higher level than the amount required by regulators and the rating agencies.

4. Cover pool

4.1 - CHANGE IN ASSETS IN 2017

The net change in the cover pool in 2017 corresponded to a decrease in assets in the amount of EUR 2.4 billion. This change is explained by the following items.

EUR billions	2017
1- Acquisition of loans from La Banque Postale	3.3
Loans to the French public sector (vanilla loans in euros)	3.3
2- Export credits drawings	0.2
Loans to SFIL to refinance export credit guaranteed by the French State	0.2
3- Reduction of loan sensitivity	0.3
Sensitive structured loans eliminated	(0.4)
Refinancing loans (vanilla loans in euros)	0.4
New loans (vanilla loans in euros)	0.3
4- Amortization of portfolio of loans and securities	(4.7)
5- Early reimbursements	(0.2)
6- Changes in treasury	(1.3)
Net change in securities investments	0.7
Net change in Banque de France cash deposit	(2.0)
7- Other changes	0.0
Net change in the cover pool	(2.4)

In 2017, Caisse Française de Financement Local acquired a total of EUR 3.3 billion in loans to the French local public sector and public hospitals originated by La Banque Postale.

Drawings on refinancing loans of large export credits granted to SFIL became effective during 2017 in the amount of EUR 0.2 billion. These loans benefit from an irrevocable and unconditional 100% guarantee by the French State.

In application of the policy of reduction of loan sensitivity in effect since the beginning of 2013, the operations conducted by SFIL in 2017 made it possible to decrease outstanding loans considered as sensitive by EUR 0.4 billion through their replacement with fixed rate loans. They were accompanied by new fixed rate loans in the amount of EUR 0.3 billion.

The natural amortization of the portfolio of loans and securities represented EUR 4.7 billion in 2017, and early reimbursements represented EUR 0.2 billion.

Available cash decreased by EUR 1.3 billion. It is deposited at the Banque de France, invested in bank bonds classified as replacement assets, invested in European public sector bonds or lent to SFIL.

There were no divestments, except for treasury investments, in 2017.

4.2 - OUTSTANDING ASSETS AS OF DECEMBER 31, 2017

Caisse Française de Financement Local's pool of assets is exclusively composed of exposures on public sector entities, or guaranteed by the same, and replacement assets (within the limits specified by current legislation).

EUR billions	12/31/2016	12/31/2017
Loans and bonds to the public sector	53.8	53.2
<i>of which large export credits refinancing⁽¹⁾</i>	-	0.2
<i>of which treasury invested in public sector bonds</i>	0.2	0.7
<i>of which other loans and bonds to the public sector</i>	53.6	52.2
Banque de France cash deposit	3.7	1.7
Replacement assets	0.7	0.9
COVER POOL	58.2	55.8
Financing commitments granted to refinance large export credits ⁽¹⁾⁽²⁾	3.7	3.0
Financing commitments granted to other public sector loans	0.1	0.1
FINANCING COMMITMENTS GRANTED	3.8	3.1

(1) For the record, loans refinancing large export credits concluded with SFIL benefit from an irrevocable and unconditional 100% guarantee granted by the French State (enhanced guarantee).

(2) In 2016, commitments granted represented EUR 3.1 billion of signed firm offers and EUR 0.6 billion of concluded contracts in drawing phase. In 2017, commitments granted represented concluded contracts in drawing phase.

Surplus cash is deposited in an account opened by Caisse Française de Financement Local at the Banque de France or invested in European public sector or bank (replacement assets) securities, respectively amounting to EUR 1.7 billion, EUR 0.7 billion and EUR 0.5 billion as of December 31, 2017. In 2017, Caisse Française de Financement Local also invested some of its surplus cash in loans granted to its parent company SFIL (replacement assets), for a total of EUR 0.4 billion as of December 31, 2017.

The amount of financing commitments given came to EUR 3.1 billion as of December 31, 2017, including EUR 3.0 billion for loans to SFIL signed but not yet drawn, in connection with the refinancing of large export credits. As a reminder, these loans benefit from an irrevocable and unconditional 100% guarantee by the French State.

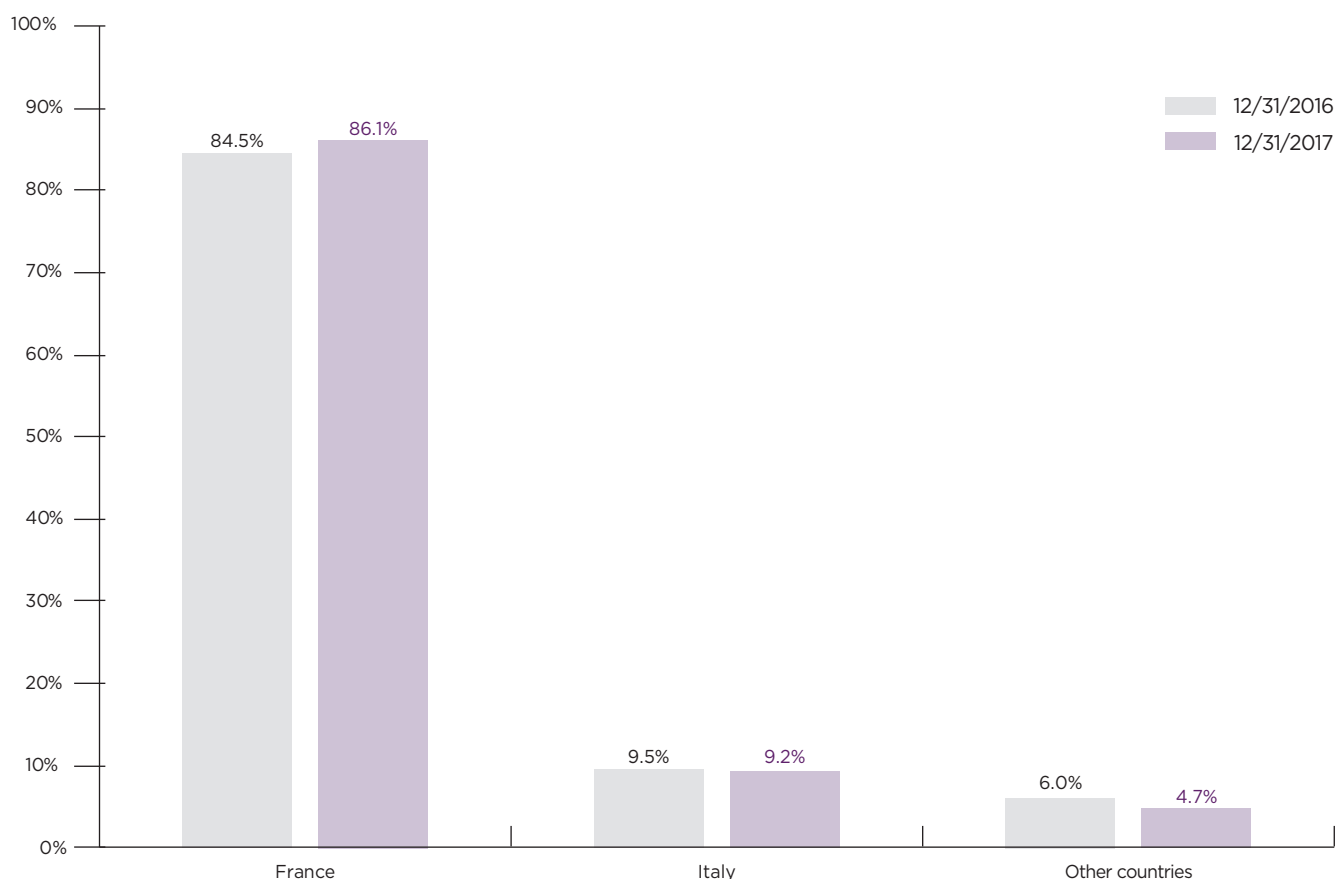
4.2.1. Public sector loans and securities (excluding replacement assets and treasury placed with the Banque de France)

4.2.1.1. Geographic breakdown

At the end of December 2017, French public sector loans made up the majority (86.1%) of the cover pool, a share due to increase in the future. They include loans acquired from La Banque Postale since 2013 for 20% (EUR 10.7 billion) and State-guaranteed loans granted to SFIL to refinance large export credits for less than 1% (EUR 0.2 billion).

The other assets are managed in a run-off mode; they correspond to granular and geographically diversified exposures on foreign public sector entities.

The relative proportion of the total assets can be broken down as follows.

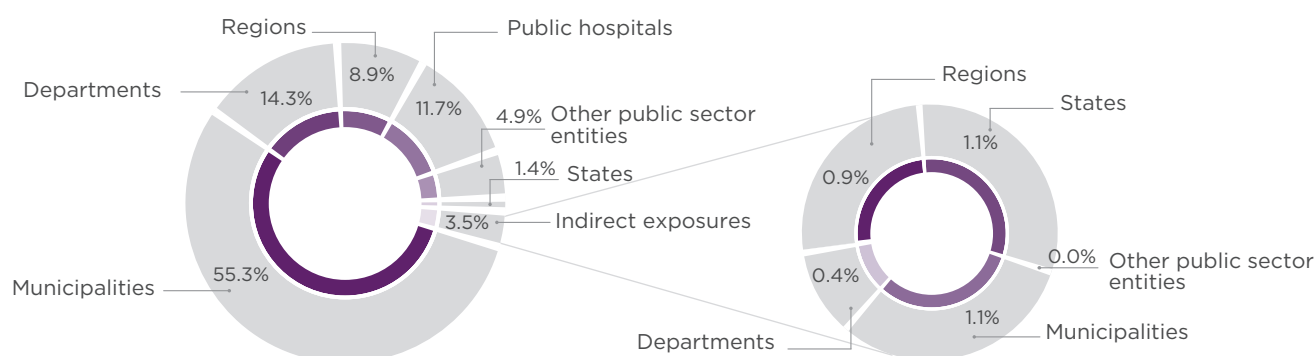


Exposures to Other countries as of December 31, 2017, are broken down by country in the section Bonds and public sector loans, which is presented at the end of this management report.

4.2.1.2. Breakdown by type of counterparty

The portfolio of Caisse Française de Financement Local is made up of the following items:

- for 81%, direct or indirect exposures on municipalities, departments or regions;
- for 12%, exposures on public hospitals;
- for 7%, sovereign exposures or commitments on other public sector entities (including public social housing).



Indirect exposures are composed of exposures guaranteed by public sector entities, most of which are local. Large export credits refinancing exposures are listed in the category of indirect exposures guaranteed by States.

4.2.1.3. Securitizations

There are no securitization units in the cover pool of Caisse Française de Financement Local (since July 2013). Its *obligations foncières* respect the conditions of eligibility for refinancing by the European Central Bank and the new CRR/CRD IV requirements.

4.2.2. Replacement assets

Assets considered by law as replacement assets correspond to exposures on credit institutions benefiting from at least a Step 1 rating, or a Step 2 rating when their remaining maturity does not exceed 100 days, and their total amount is limited to 15% of *obligations foncières* and registered covered bonds.

As of December 31, 2017, replacement assets represented 1.8% of *obligations foncières* and registered covered bonds. The Caisse Française de Financement Local's cash surplus can be invested in banking sector securities (in addition to deposits at the Banque de France and investments in European public sector securities) or lent to SFIL. In this case, bank exposures are classified as replacement assets, broken down below based on the rating of the issuers. In addition, Caisse Française de Financement Local granted two loans to SFIL to invest its surplus cash. These loans are also included in the replacement assets.

Replacement assets EUR millions	Country	12/31/2016	12/31/2017
Step 1 credit rating			
Covered bonds			
	France	26	176
	Other countries ⁽¹⁾	-	127
Other bank bonds			
	France	120	148
	Other countries ⁽¹⁾	-	100
Loans to parent company, SFIL	France	-	360
Step 2 credit rating			
Bank bonds (maturity < 100 days)			
	France	500	-
	Other countries ⁽¹⁾	-	-
Bank accounts balances	France and Other countries ⁽¹⁾	4	10
TOTAL		650	921

(1) Corresponds to other countries of the European Union and the European Economic Area, except for bank accounts, which can be held in non-European countries

4.2.3. Assets removed from the cover pool

Because of its status as a credit institution, Caisse Française de Financement Local has access to refinancing operations offered to banks by the Banque de France within the Eurosystem. In steering its cover pool and its over-collateralization or in order to meet the need for temporary liquidity, Caisse Française de Financement Local may thus convert a portion of its assets into cash. The loans or securities assigned in guarantee with the central bank in order to obtain financing on the occasion of tenders organized by the Banque de France are then taken out of the cover pool and replaced by the cash thus obtained.

The same treatment would be applied to the assets in the cover pool if they were mobilized in interbank repurchase agreements in the event of a need for liquidity.

During the last three fiscal years, in the context of the regular tests of its operational procedures for accessing refinancing from the Banque de France or bank counterparties, Caisse Française de Financement Local has mobilized assets of very small unit amounts.

4.2.4. Structured loans

4.2.4.1. Definition

Certain loans to French public sector entities in the cover pool of Caisse Française de Financement Local may be qualified as structured loans. To define this notion, Caisse Française de Financement Local refers to the charter of good practices signed by banks and local governments (the Gissler charter), which can be consulted on the Internet site of the French Ministry of the Interior⁽¹⁾. This document was signed on December 7, 2009, by several organizations that represent local governments in France (Association des maires de France, Fédération des maires des villes moyennes, Association des petites villes de France, Association des maires de grandes villes de France and Assemblée des communautés de France) as well as certain banks.

Therefore, structured loans are defined as:

- all the loans with structures belonging to Gissler charter categories B to E;
- all the loans “outside the charter”, the commercialization of which is excluded by the charter, either because of their structure (leverage > 5, etc.), their underlying index(es) (foreign exchange, etc.), or their currency (loans denominated in CHF, JPY, etc.);

The most structured loans according to the Gissler classification (categories 3E, 4E and 5E as well as loans which the charter does not allow to be marketed) may be qualified as “sensitive”. They are closely monitored and specific measures are taken to reduce their sensitivity. They benefit from support from funds set up by the French government in order to allow customers to convert sensitive loans into fixed rate vanilla loans.

4.2.4.2. Part of structured loans in the cover pool

EUR billions	Outstanding				Number of customers ⁽¹⁾		
	12/31/2016	12/31/2017	Change	% cover pool	12/31/2016	12/31/2017	Change
French public sector loans	44.8	45.0	0.2	80.7%	16,335	15,366	(969)
Vanilla loans	38.4	39.6	1.2	71.0%	14,578	13,720	(858)
Structured loans	6.4	5.4	(1.0)	9.7%	1,757	1,646	(111)
Sensitive loans not in the charter	0.7	0.6	(0.1)	1.1%	85	64	(21)
Sensitive loans (3E/4E/5E)	1.0	0.8	(0.2)	1.4%	189	162	(27)
Subtotal sensitive loans:	1.7	1.4	(0.3)	2.5%	274	226	(48)
Structured loans benefiting from the derogatory mechanism of the support fund	0.7	0.5	(0.2)	0.8%	83	71	(12)
Other structured loans	4.0	3.5	(0.5)	6.3%	1,400	1,349	(51)

(1) considering the customer in the category with its most highly structured loan

In 2017, outstanding loans to the French public sector have increased by EUR 0.2 billion, with a EUR 1.2 billion increase in non-structured loans (vanilla) and a decrease of EUR 1.0 billion in structured loans (see the definition above).

At the end of 2017, structured loans on the balance sheet of Caisse Française de Financement Local represented EUR 5.4 billion.

4.2.4.3. Sensitive loans

Sensitive loans, which are the most structured, totaled EUR 1.4 billion as of December 31, 2017, compared with EUR 1.7 billion as of December 31, 2016.

Of these loans, those considered to be the most sensitive (outside the charter) represented EUR 0.6 billion, or 1.1% of the cover pool and 64 customers on December 31, 2017. In particular, this portfolio included loans indexed on the EUR/CHF exchange rate. This portfolio concerns the following customer categories.

Sensitive loans not in the charter EUR billions	12/31/2016		12/31/2017	
	Amounts	Number of customers	Amounts	Number of customers
Municipalities with fewer than 10,000 inhabitants	0.0	6	0.0	5
Municipalities with more than 10,000 inhabitants and groups of municipalities	0.3	50	0.2	34
Regions and departments	0.1	9	0.2	9
Public hospitals	0.3	17	0.2	14
Other customers	0.0	3	0.0	2
TOTAL	0.7	85	0.6	64

(1) http://www.interieur.gouv.fr/content/download/3021/30417/file/Charte_de_bonne_conduite_entre_les_etablissements_bancaires_et_les_collectivites_territoriales.pdf

The 64 customers are mostly municipalities with a population of more than 10,000 inhabitants and groups of municipalities, and to a lesser extent, public hospitals. There are five municipalities with a population less than 10,000 inhabitants with a sensitive loan “not in the charter” and the outstanding loans concerned by these municipalities total almost zero. At the end of 2017, more than 93% of the borrowers with loans indexed on EUR/CHF saw loan sensitivity disappear completely, and of this number, 96% were small local governments and hospitals.

4.2.4.4. Reduction in loan sensitivity

Proactive sensitivity reduction measures, the use of support funds and, to a lesser extent, the maturing of certain loans made it possible to reduce the number of sensitive customers by 653 between SFIL's launch and December 31, 2017. The number of customers holding sensitive loans decreased from 879 to 226, and the outstanding sensitive loans dropped from EUR 8.5 billion to EUR 1.4 billion (2.5% of the cover pool), i.e. a decrease of more than 83%.

This decrease includes EUR 0.5 billion that represents outstanding loans for which the customers chose to maintain their sensitive loan temporarily, while having the option of receiving aid from the local government support fund if the structured component of their loan becomes activated (system for helping pay interest at a degraded rate provided for by the support fund doctrine). The loans concerned by this option mainly correspond to loans with an interest rate based on leverage and which are, at this time, most often at fixed rates because the structured component is not or has never been activated.

Based on transactions already entered into, total sensitive structured loans will be reduced to EUR 1.2 billion by the end of 2018, of which a maximum of EUR 0.6 billion relating solely to local government entities. On the same basis, by end-2018, sensitive loans with an activated structured component and a rate exceeding 5% will amount to less than EUR 0.2 billion and will concern 34 customers, i.e. 0.4% of the cover pool and 0.2% of customers in the French local public sector.

5. Debt benefiting from the legal privilege

As of December 31, 2017, debt benefiting from the legal privilege is composed of *obligations foncières* and registered covered bonds issued by Caisse Française de Financement Local as well as of cash collateral received from counterparties in derivative transactions.

EUR billions	12/31/2016	12/31/2017
Cash collateral received	1.3	0.7
<i>Obligations foncières</i> and registered covered bonds	50.4	49.0
TOTAL	51.7	49.7

5.1 - CHANGE IN CASH COLLATERAL

Cash collateral received by Caisse Française de Financement Local decreased compared with the situation at the end of December 2016. Its level stood at EUR 0.7 billion at the end of December 2017.

5.2 - CHANGE IN ISSUES

Within the recurrent annual program of EUR 5 billion to EUR 7 billion, the issuance policy of Caisse Française de Financement Local primarily aimed to construct a coherent yield curve in the euro market while keeping an eye on the good performance of its benchmarks in the secondary market. The diversification of its sources of financing is necessary to achieve long maturities coherent with its needs. This implies an active presence in the market of private placements within the framework of the EMTN program or the issue of registered covered bonds.

5.2.1. New issues in 2017

In 2017, Caisse Française de Financement Local achieved a volume of issues of EUR 6.0 billion by enhancing its reference curve with four new points, by increasing the amount of existing *souches* (taps) and by continuing to work in the private placement segment.

Caisse Française de Financement Local raised money in the primary market on three occasions for a total amount of EUR 4.0 billion:

- a 10-year issue in January for EUR 1.5 billion;
- a dual tranche issue (7 and 15 years) in May for a total amount of EUR 1.75 billion;
- a 10-year issue in September for EUR 0.75 billion.

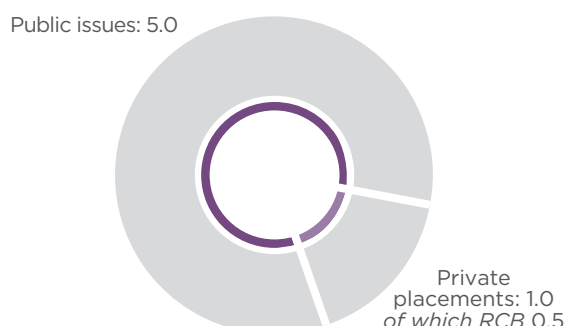
At the same time, Caisse Française de Financement Local provided additional liquidity for several of its reference issues via six taps in 2017 for a cumulated amount of EUR 1.0 billion.

In addition to these public transactions, Caisse Française de Financement Local remained active in the private placement segment and especially with the registered covered bond (RCB) format, thus making it possible to respond to investors' search for long and very long maturities. A total of EUR 1.0 billion was raised in this market segment, of which more than 60% on maturities of 20 years or more.

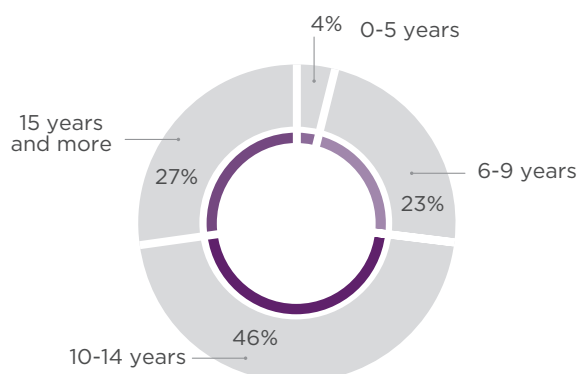
The weighted average life of 11.3 years for 2017 issues made for an excellent match between assets and liabilities.

The breakdown of new issues by public/private format and maturity is presented below, as well as the breakdown of public issues by investor category and geographic zone.

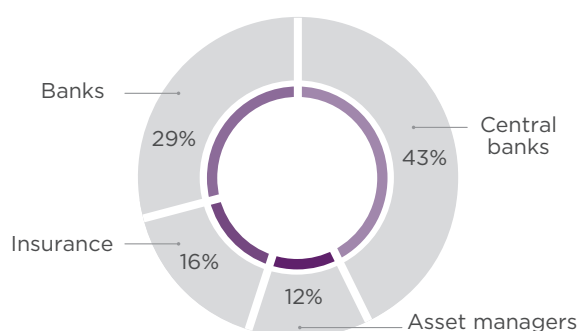
**Breakdown of 2017 issues
by format**
EUR billions



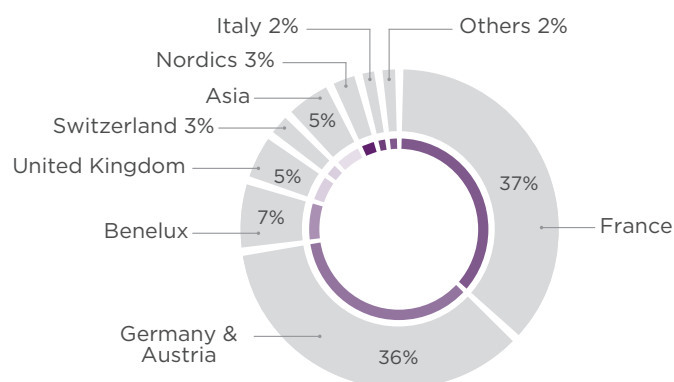
**Breakdown of 2017 issues
by maturity**
%



**Breakdown of 2017 public issues
by investor category**
%



**Breakdown of 2017 public issues
by geographic zone**
%



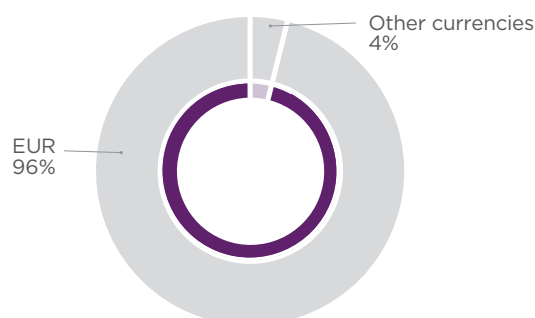
5.2.2. Outstanding debt as of December 2017

Outstanding *obligations foncières* and registered covered bonds totaled EUR 49.0 billion in swapped value at the end of December 2017. This includes new issues of *obligations foncières* for EUR 6.0 billion and amortization of issues maturing in 2017 for EUR 7.2 billion.

Limited buybacks of *obligations foncières* were performed over the year in order to smooth out the amortization profile of Caisse Française de Financement Local's privileged debts.

EUR billions value after currency swap	2016	2017
BEGINNING OF THE YEAR	51.6	50.4
Issues	5.9	6.0
Amortizations	(7.0)	(7.2)
Buyback	(0.1)	(0.2)
END OF THE YEAR	50.4	49.0

As of December 31, 2017, issues can be broken down by currency as follows:



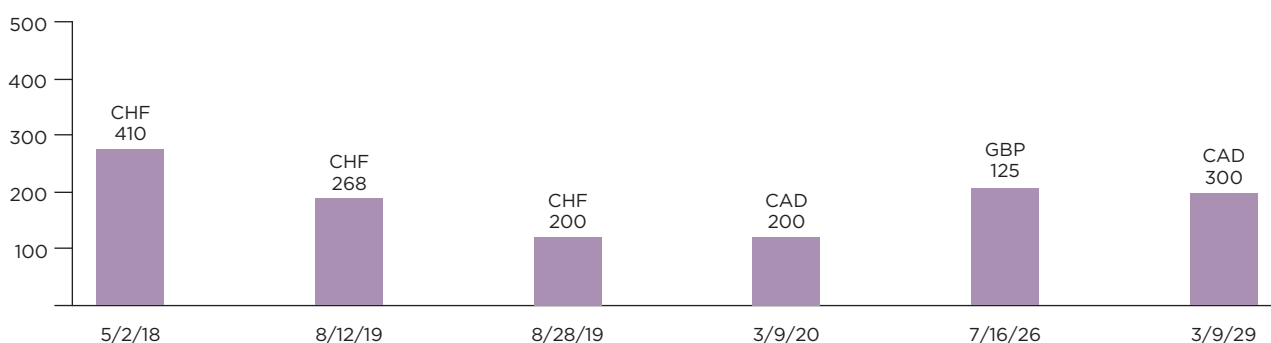
Breakdown of benchmark tranches in EUR

EUR millions



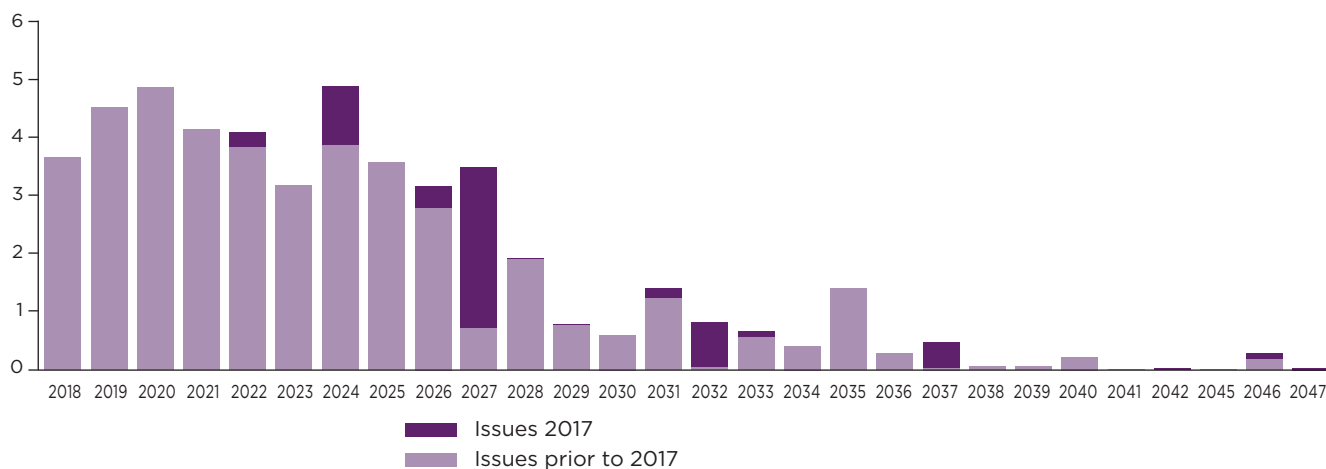
Main tranches in other currencies

value in EUR millions
(swapped value)



Amortization of obligations foncières and registered covered bonds

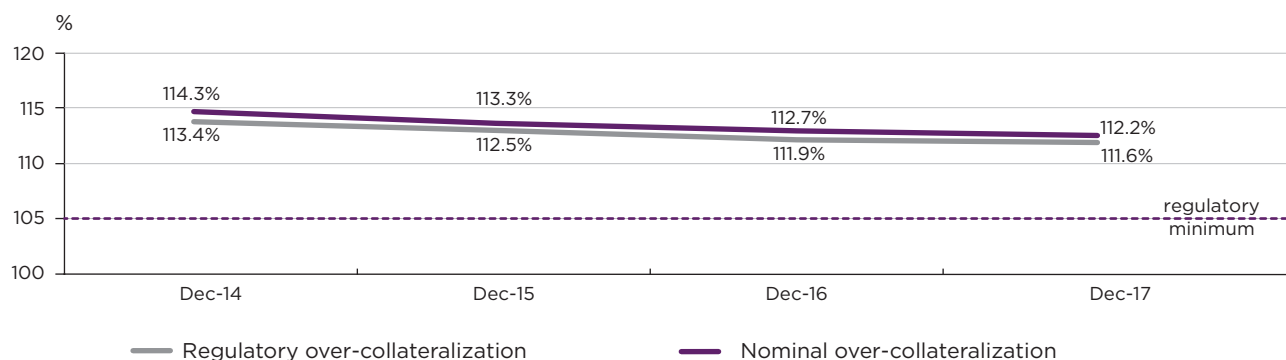
En EUR billions



6. Changes in the over-collateralization ratio

The over-collateralization ratio, which is calculated on the basis of regulatory standards governing *sociétés de crédit foncier*, is the ratio between the assets and the resources benefiting from the legal privilege. The legal minimum threshold is set at 105% and corresponds to the minimum level that Caisse Française de Financement Local had committed to maintain since its creation.

In practice, the over-collateralization ratio is regularly higher than 105%. To maintain an adequate level of credit rating, a level of over-collateralization of more than 5% may be required. This requirement depends on the method applied by each of the rating agencies and on the new assets and liabilities on Caisse Française de Financement Local's balance sheet and it may vary over time. Caisse Française de Financement Local takes these particular requirements into account in the management of its activity in order to make sure they are constantly met and strives to maintain its over-collateralization at a relatively stable level, as can be seen in the following graph.

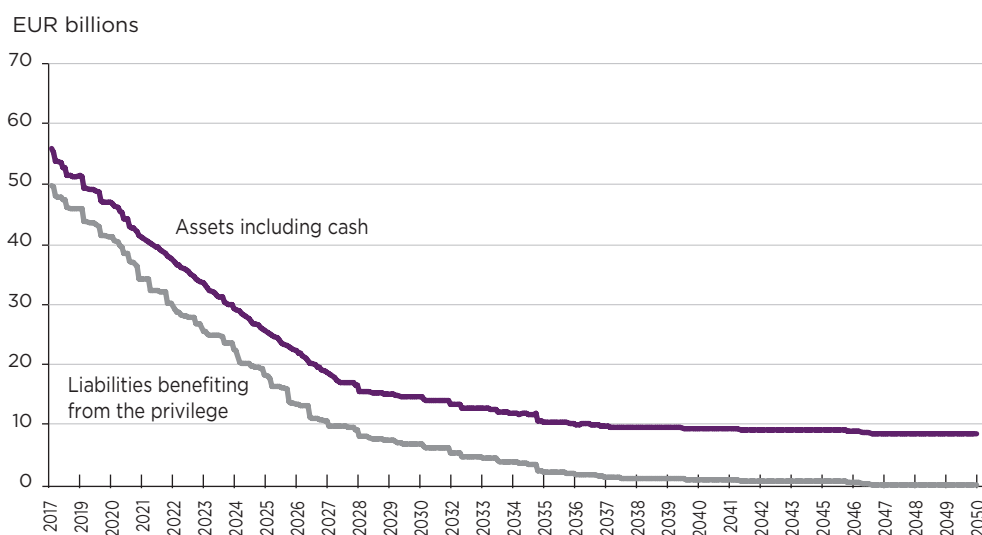


Regulatory over-collateralization may differ from nominal over-collateralization. In fact, it is calculated on the basis of the rules determined by the Autorité de contrôle prudentiel et de résolution (ACPR). In particular, these rules require different weighting levels according to the assets. The assets in Caisse Française de Financement Local's cover pool are weighted at 100%. The small difference between the two ratios can be explained by the accrued interest not yet due taken into account in the regulatory over-collateralization ratio.

Any assets that Caisse Française de Financement Local may have assigned in guarantee to borrow funds from the Banque de France or any other banking institution would be excluded from the calculation of over-collateralization.

Over - collateralization may also be illustrated by the gap between the amortization curves of the assets and liabilities benefiting from the privilege. The following graph presents the curves as of December 31, 2017.

Amortization of assets and liabilities as of December 31, 2017



In this graph, the assumption is made that excess cash generated over time is included in the cover pool.

7. Change in debt that does not benefit from the legal privilege

The asset surplus (assets exceeding *obligations foncières* and registered covered bonds) and miscellaneous needs are financed by equity and debt that does not benefit from the privilege of the law on *sociétés de crédit foncier*.

Such financing is obtained through the parent company. At the end of December 2017, the funds borrowed from SFIL within the framework of the financing agreement were made up of different loans with maturities that could initially run from one day to ten years with an Euribor or Eonia index.

Temporary financing may also be obtained from the Banque de France. These funds do not benefit from the privilege stipulated in the law on *sociétés de crédit foncier*, but they are guaranteed by loans and securities assigned for this purpose in the account of Caisse Française de Financement Local at Banque de France. Since the creation of SFIL, except when it used

small sums to test the access procedure for such funding, Caisse Française de Financement Local has not contracted any loans from the Banque de France or from credit institutions other than its parent company.

The change in financing that does not benefit from the legal privilege, excluding accrued interest not yet due, can be presented as follows.

EUR billions	12/31/2016	12/31/2017
SFIL	5.2	4.8
Banque de France	-	-
TOTAL	5.2	4.8

8. Internal Control and Preparation of accounting and financial information

8.1 – GENERAL DESCRIPTION OF THE INTERNAL CONTROL PROCEDURES

8.1.1. Responsibilities of internal control and the general architecture of internal control

SFIL, with its subsidiary Caisse Française de Financement Local, is one of the large banks that has been under the direct supervision of the European Central Bank (ECB) since November 2014 in the framework of the Single Supervisory Mechanism (SSM). In addition, as a *société de crédit foncier*, Caisse Française de Financement Local is subject to special and additional oversight by the Autorité de contrôle prudentiel et de résolution (ACPR).

Since it manages Caisse Française de Financement Local, SFIL has been delegated to exercise the functions of internal control for Caisse Française de Financement Local pursuant to its management agreement. Consequently, internal control at SFIL also meets the regulatory obligations of Caisse Française de Financement Local in this regard.

The objectives and organization of SFIL's internal control are defined within the framework set by the Monetary and Financial Code, and by the *arrêté* of November 3, 2014. According to these articles, the internal control system requires that different control procedures are applied to provide:

- a control system for operations and internal procedures;
- an organization of financial and accounting data;
- systems to measure risks and results;
- systems to monitor and control risks;
- a system for documentation and information;
- surveillance of flows of cash and securities.

This internal control system is a process put into practice by Executive Management and all the employees of SFIL, at the initiative of its Board of Directors. The organization is designed to provide reasonable but not absolute assurance with regard to the achievement of the objectives that SFIL set in terms of performance, profitability and protection of its financial assets.

Specifically, the objectives assigned to internal control in effect at SFIL on behalf of Caisse Française de Financement Local aim to:

- verify the efficiency of risk control procedures. It aims to guarantee that the risks taken by the Company are in line with the policy defined by the Supervisory Board and the Executive Board and do not exceed an agreed-upon level of risk;
- ensure that the financial and accounting data produced is reliable and relevant. The main objective of the financial information is to give a true and fair view of the position of Caisse Française de Financement Local in a regular, complete and transparent manner;
- monitor compliance with internal and external rules and practices of business ethics. The diligent operation of Caisse Française de Financement Local implies strict respect of legislative and regulatory obligations, in particular with regard to corporate governance and compliance;
- monitor the effectiveness and operational efficiency of processes, in order to ensure that operations are carried out properly while guaranteeing efficient management of available resources.

In order to allow the accomplishment of the objectives set, and in compliance with the *arrêté* of November 3, 2014, the general architecture of the internal control system of SFIL is based on three levels of control:

- the first control level takes place in the operating teams;
- the second level corresponds to the permanent control activities carried out under the responsibility of the Operational Risks and Permanent Control division or, for non-compliance risks, the Compliance division (in the four compliance areas: organization of compliance, ethics and markets integrity, protection of customer interests and financial security);
- the third control level concerns periodic control conducted by an independent team, the Internal Audit and Inspection division, which reports to the Chief Executive Officer of SFIL and which exercises periodic oversight of the efficient and effective application of the two above-mentioned levels of control.

The different functions in charge of internal control (Operational Risks and Permanent Control division, Compliance division and Internal Audit and Inspection division) meet every quarter in an Internal Control Committee in order to share information about the risks each division has identified in its field of competence, to coordinate internal control initiatives so as to remedy risk situations and analyze the conclusions in their respective control plans.

If they deem it necessary, the heads of internal control functions report to SFIL's Chief Executive Officer and its Board of Directors. They report regularly to the appropriate board committee, the Risks and Internal Control Committee. They may be heard by this committee at their request and can report directly to the Board of Directors if they believe that a potentially significant event should be brought to its attention. These managers may not be terminated without the approval of the Board of Directors. If these missions or events concern Caisse Française de Financement Local, these managers report to the Executive Board and, if necessary, to the Supervisory Board.

These different levels of control are deployed under the aegis of the supervisory and management bodies of SFIL and Caisse Française de Financement Local.

8.1.2. Executive Board of Caisse Française de Financement Local

The Executive Board of Caisse Française de Financement Local is the front-ranking guarantor of the efficient operation of the Company's internal control procedures. In light of the structure of Caisse Française de Financement Local and of the management agreement which binds it to its parent company, the Executive Board relies on the governance and organization of internal control in effect at SFIL.

- The Risks and Internal Control Committee, which is composed of the members of the Board of Directors of SFIL, is responsible, in keeping with the Code of Commerce and the *arrêté* of November 3, 2014, for ensuring the efficiency of internal control and risk management systems, giving an appreciation of the quality of internal control, in particular the coherence of measurement, surveillance and risk control systems, and suggesting, if need be, any additional action. This committee is also responsible for monitoring permanent control, compliance and periodic control at SFIL. It likewise examines, with the Company's auditors, any risks weighting on their independence.
- SFIL's Chief Executive Officer and its Deputy Chief Executive Officer are considered as accountable officers by banking regulators. They guarantee the efficient operation of the bank's internal control system. They allocate the resources required to carry out the missions of the different divisions in charge of control, verify that the objectives are attained and that the internal control system is adapted to the needs of SFIL and Caisse Française de Financement Local. To this end, they regularly receive activity reports and the results of the controls carried out in terms of permanent control, compliance and periodic control. These reports are also presented and discussed at meetings of SFIL's Executive Committee, and the issues raised engender action and decisions in order to ensure continuous improvement in internal control.

8.1.3. First level of control: operating divisions

As the first level of the internal control system, employees and managers of SFIL's operating divisions are in charge of analyzing the risks involved in all the transactions they have initiated, organizing and conducting first-level controls for such operations, verifying that internal control procedures in their division are adapted to such risks and contributing to their development. To this end, they rely on the policies, procedures, systems, limits and indicators with a clear separation between the launch of operations and their validation, control or settlement. These policies, procedures, systems, limits and indicators are defined by several specialized committees. They are composed of operating, support, and control staff, and chaired by a member of the Executive Committee of SFIL.

8.1.4. Second level of control: first pillar - permanent control excluding compliance

Permanent control excluding compliance ensures the reliability of the system of risk control, the efficiency of the control of operations and internal procedures, the quality of accounting and financial information and of IT systems.

8.1.4.1. Organization and governance

The permanent control system (excluding compliance) applies to all divisions and activities. It is operated by the Operational Risks and Permanent Control division, part of the Risks division, in such a way as to maintain synergies with the operational risk management, IT security and business continuity systems. The system relies on both the Operational Risks and Permanent Control division, which performs certain second-level controls, and a network of operating division correspondents tasked with performing and monitoring certain controls and reporting thereon to the Operational Risks and Permanent Control division.

8.1.4.2. Activities

The management principles governing permanent control, excluding compliance, are described in the management policy for operational risks and permanent control. Permanent control is based on a control plan which is prepared in collaboration with the operating divisions and covers the range of SFIL's activities. It is reviewed every year. The objective of this review is to adapt the controls to the situation at SFIL by taking into account:

- the results of controls carried out during the year (their match with the risks to be covered, their efficiency, their formalization and the pertinence of related measurement indicators);
- the review of incidents noted;
- the recommendations of the internal audit division, the statutory auditors and the regulator;
- new products and processes at SFIL.

Thus, efforts to ensure continuous improvement make it possible to develop the control plan by adapting existing controls, while adding new ones and removing controls which are redundant or no longer relevant.

The Operational Risks and Permanent Control division and its correspondents conduct or evaluate controls within their scope at a pre-determined frequency based on the criticality of the underlying risks (usually quarterly but in some cases semi-annually).

ally or annually). This evaluation is documented by a commentary and supporting documentation. The results of the controls, conducted or evaluated by correspondants, are reviewed by the Operational Risks and Permanent Control division, which may validate or refuse them, particularly in the latter case if the documentation is deemed insufficient. In the event the control results are unsatisfactory, action plans are systematically put in place to obtain a satisfactory result for subsequent periods. These action plans are regularly monitored and a quarterly report is submitted to the Operational Risks and Permanent Control Committee.

At the end of 2017, 133 permanent controls were in place.

8.1.4.3. Reporting

The accountable officers, the members of the Executive Committee and of the Board of Directors are kept regularly informed of permanent control activities through the Risk and Internal Control Committee. The same is true for the Executive and Supervisory Boards of Caisse Française de Financement Local.

The Operational Risks and Permanent Control division publishes a quarterly report presented to the Operational Risks and Permanent Control Committee. This Committee is chaired by the Deputy Chief Executive Officer of SFIL and is made up of all the members of SFIL's Executive Committee. The Chairman of the Executive Board of Caisse Française de Financement Local also takes part. The Committee meets quarterly to review the permanent control system: results of control evaluations, monitoring of action plans, review of control frequencies, additions, deletions or changes of controls. It also looks at the main issues linked to permanent control and at areas of anticipated improvements. The main points which are recognized are presented to the Risk and Internal Control Committee by the head of the Risks division as part of the Quarterly Risk Review.

The Risks and Internal Control Committee meeting of January 25, 2018 and the Executive Board meeting of February 13, 2018 were informed of the control results, focus points, corrective actions to be implemented and permanent control improvements achieved in 2017.

8.1.5. Second level of control: second pillar - compliance control

8.1.5.1. Organization and governance

The Compliance division is responsible for managing compliance risk, as defined in article 10 of the *arrêté* of November 3, 2014, for all of SFIL's and Caisse Française de Financement Local's activities. The aim of compliance risk management is to ensure compliance with:

- laws, regulations, professional conduct rules and directives;
- measures to protect the reputation of the Group, its investors and its customers;
- ethical rules relating to business practices, and measures to prevent conflicts of interest, protect customers' interests and maintain markets integrity;
- anti-money laundering, corruption and financing of terrorism measures, and financial embargoes.

Pursuant to article 29 of the *arrêté*, SFIL's Compliance division is autonomous, independent of all operational units and particularly of any commercial activity. It reports to SFIL's General Secretary, Chief Compliance Officer, Executive Committee member and SFIL's and Caisse Française de Financement Local's designated compliance control manager for relations with the ACPR. Reporting directly to SFIL's Chief Executive Officer, the General Secretary has direct and independent access to the company's Risks and Internal Control Committee and Board of Directors. The General Secretary also acts as the TRAC-FIN correspondent in connection with the bank's anti-money laundering and financing of terrorism obligations.

8.1.5.2. Compliance control activities

To ensure that the system for managing SFIL's and Caisse Française de Financement Local's non-compliance risks is effective, the Compliance division implements a control plan aimed at containing and, if possible, eliminating non-compliance risks.

This control plan is based on the non-compliance risk mapping and is updated at least annually to take into account changes in SFIL's and Caisse Française de Financement Local's internal and external environments.

The Compliance division implements and documents compliance controls in accordance with the control plan. Specific action plans sent to the divisions responsible for implementing remediation actions are systematically implemented in the event of malfunctions identified by the controls. The Compliance division monitors these action plans and their overall progress.

The Compliance division updates the non-compliance risk mapping and the resulting control plan as necessary to take into account changes in SFIL's activity and those arising from the entry into force of new regulations. The methodology for rating «gross» and «net» non-compliance risks is identical to the internal audit methodology. The updated non-compliance risk mapping and control plan are submitted every January for approval by the Risks and Internal Control Committee. The 2018 non-compliance risk mapping and control plan were presented to and approved by the Risks and Internal Control Committee on January 25, 2018. Caisse Française de Financement Local's Executive Board was also informed of the non-compliance risk mapping and control plan update on February 13, 2018.

Lastly, the Compliance division uses various internal tools to report shortcomings, breaches and malfunctions: a network of compliance correspondents, a professional and ethical alert procedure and an incident reporting system.

8.1.5.3. Reporting

SFIL's and Caisse Française de Financement Local's accountable officers, the members of SFIL's Executive Committee and Board of Directors and of Caisse Française de Financement Local's Supervisory Board are regularly kept up to date with the

compliance system. The Compliance division submits a semi-annual report to the Executive Committee, Caisse Française de Financement Local's Executive Board and the Risks and Internal Control Committee presenting the results of its activities and controls, including compliance control results, action plan monitoring, and the compliance risk mapping and annual control plan. The Executive Committee issues an opinion on the compliance system's main issues and broad areas for improvement.

Lastly, every year the Compliance division makes a presentation and submits an annual activity report to a special Risks and Internal Control Committee meeting excluding general management, to which the risk, compliance and periodic control officers contribute. In respect of the 2017 fiscal year, this presentation was made at the Risks and Internal Control Committee meeting of January 25, 2018, and the Executive Board was informed of the compliance control results and improvements achieved in 2017 at its meeting of February 13, 2018.

8.1.6. Third level of control: periodic control

The periodic control of Caisse Française de Financement Local, which is ensured by SFIL, involves internal audit and inspection.

8.1.6.1. Organization and governance

Periodic control, in the sense of the *arrêté* of November 3, 2014, is exercised by the Internal Audit⁽¹⁾ and Inspection⁽²⁾ division which is under the responsibility of the General Auditor. The scope of this function covers all the activities, operating processes and systems of the SFIL Group with no reserve or exception, including externalized essential activities and anti-fraud techniques. The independence and efficiency of the internal audit and inspection function are guaranteed by several factors:

- the General Auditor's direct reporting to SFIL's Chief Executive Officer;
- the absence of involvement in the operating management of SFIL's activities;
- unconditional, immediate access to all information, documents, premises, systems or persons its activities require;
- the resources made available by Executive Management to carry out these missions;
- the respect of the principles of integrity, objectivity, confidentiality and competence (through a permanent training plan to inculcate audit techniques and regulatory developments) on the part of the staff of the internal audit division.

These principles are reflected in the internal audit charter and the inspection charter, approved by the SFIL Risks and Internal Control Committee meeting of January 26, 2017, and distributed to all SFIL employees to remind them of the rights and duties of the auditors and the auditees.

More specifically, the General Auditor of SFIL exercises a particular function concerning Caisse Française de Financement Local, as spelled out in article 5.8 of the management agreement between Caisse Française de Financement Local and SFIL. SFIL's Internal Audit division audits all of the transactions and procedures of Caisse Française de Financement Local. It also provides periodic control in Caisse Française de Financement Local's internal control.

It ensures that all the risks incurred by Caisse Française de Financement Local are covered by:

- the identification of these risks and the periodic evaluation of the internal control environment;
- the planning and accomplishment of internal audit missions;
- the coordination of regulatory authorities' audits;
- the follow-up on recommendations;
- investigations (preventive measures, awareness and detection of fraud).

The General Auditor has direct access to the Chairman of the Supervisory Board of Caisse Française de Financement Local.

As of January 1, 2018, the Internal Audit and Inspection division counted nine positions (plus two alternates), including six auditors and audit managers. The General Auditor supervises all audit activities and reports issued by the department. The General Auditor is assisted by a Supervisor, who is in charge of the team of auditors and oversees the audit missions carried out by the auditors under the responsibility of the audit managers. In addition, every auditor and audit manager is responsible for a specific field through permanent documentation, risk oversight, and the monitoring of recommendations for implementation by SFIL's operating divisions.

8.1.6.2. Activities

Activities in this area are described in an internal audit brochure that is regularly updated and based on the reference framework of the professional internal audit practices of IFACI (Institut Français de l'Audit et du Contrôle Interne). The last update of this manual dates from June 2017. In order to monitor the efficiency and performance of these activities and to identify opportunities for improvement, quantitative and qualitative indicators were introduced and are regularly measured.

Internal Audit and Inspection has adopted a top-down approach for the annual evaluation of risks, in line with the recommendations of the Institute of Internal Auditors. It is based on the identification of SFIL's objectives, then on a study of risks that are critical to the success of such goals.

In 2017, an annual assessment of risks was carried out in the second half and it gave rise to an update of the mapping of the major risks of SFIL and Caisse Française de Financement Local. This map was compared to the similar information culled in 2016. Based on this mapping, Internal Audit and Inspection prepared its 2018 map and multi-year audit and inspection plan.

(1) Internal audit is an independent and objective activity which assures SFIL of the degree of control of its operations, contributes advice on how to improve, and creates value added. It helps the organization to reach its objectives by applying a systematic and methodical approach to evaluate its risk management, control and governance processes and by making proposals to reinforce their efficiency.

(2) In the SFIL Group, inspection activities work in an independent and objective manner to enhance control of the risk of fraud.

This plan was approved by the Risks and Internal Control Committee on January 25, 2018, and by the Executive Board on February 13, 2018. The Supervisory Board is also informed on a yearly basis.

SFIL's multi-year audit plan, which is reviewed every year, is broken down into audit missions that are conducted throughout the year on the basis of a pre-established schedule and budget, depending on audit resources. These different missions include four main stages (preparation, accomplishment, conclusion and finalization). The audit methodology, which is based on IFACI methodology, was reviewed in terms of operating efficiency and in particular to focus on the significant risks identified within the audited scope. Audit missions are carried out using the methods described in a Company brochure on internal audits that is regularly updated and based on the reference framework of the professional internal audit practices of IFACI. The latest update of this manual was in June 2017.

In 2017, internal audit assignments focused on themes related to the SFIL Group's core business (management of French local public sector debt), key operational processes (corporate governance, cash management, financing provided by SFIL's shareholders) or support processes (training management, logistics and security processes), risk monitoring and internal models (recovery plan, managing derivatives-related operational risk), the information system (management of local applications) and outsourced services. The 2017 audit plan was 83% completed, exceeding the initial objective of 80%. The findings of each of these assignments and the associated recommendations were presented to the Risks and Internal Control Committee on September 5, 2017, and January 25, 2018, as well as to the Executive Board of Caisse Française de Financement Local on August 31, 2017, and on February 13, 2018.

The follow-up on recommendations made after the missions organized by Internal Audit and Inspection, oversight bodies or the Company auditors, as is the case, is carried out in a continuous and automated process to monitor the deployment of action plans resulting from these recommendations. Responsibility for the appropriate implementation of the recommendations is incumbent on identified managers. The follow-up of this implementation is under the responsibility of the auditors and audit managers in function of their field of competence. The validation of the stage of progress or accomplishment of these action plans is the responsibility of the Supervisor and the General Auditor. All of these recommendations prompted continuous monitoring in 2017 and official reports based on the situations as of May 31 and October 31, 2017, as well as presentation to the Executive Committee (in July 2017 and January 2018), the Risks and Internal Control Committee on September 5, 2017, and January 25, 2018, and the Executive Board of Caisse Française de Financement Local on February 13, 2018.

Internal Audit and Inspection is also in charge of the preparation, organization, and follow-up of the missions regulatory authorities carried out at SFIL. It also coordinates the preparation of responses to reports and the monitoring of action plans subsequent to the recommendations made.

In addition, under the aegis of the Chairman of the Financial Statements Committee and the Risks and Internal Control Committee, Internal Audit and Inspection ensured the organization of all the meetings of these committees. It oversees the respect of deadlines in the transmission and communication of information and files required for decision-making. It monitors the annual program of works set out by the Chairman of these committees. It also provides the minutes that are drawn up at each of the meetings in close cooperation with the Chairman of the committee. Lastly, it has responsibility for the safe storage of the minutes. In 2017, Internal Audit and Inspection organized six meetings for the Risks and Internal Control Committee and four for the Financial Statements Committee.

Finally, Internal Audit and Inspection is also in charge of inspection at SFIL. The purpose of this function is to play a role in the prevention, detection and investigation of fraud and to propose corrective measures in the event of dysfunctions. This unit may also respond to particular requests from the Company's legal division to provide information that may serve corporate interests. SFIL's Executive Management may also solicit the function of inspection to carry out missions and address certain specific issues. In 2017, inspection services focused on the rules governing the staff's use of SFIL's resources, access to sensitive computer applications and sensitive directories.

8.1.6.3. Reporting

SFIL's Executive Committee is kept regularly informed of internal audit and inspection activities. In particular, the audit plan is presented every year for information after discussion with SFIL's Executive Management. Every audit mission is discussed (scope, objectives, planning, etc.) for information and commentary before it effectively takes place, and its conclusions are presented for discussion and decision *via* a report which comprises:

- a general assessment regarding the subject of audit;
- an evaluation of residual risks to enable the Executive Committee to validate their match with SFIL's risks profile;
- recommendations to improve the efficiency of processes and internal controls.

A report on the follow-up of the recommendations of internal audit, inspection, oversight bodies and statutory auditors as well as the implementation of related action plans is likewise presented every six months.

The internal audit charter and the charter of inspection activities are submitted for validation to the Risks and Internal Control Committee. The audit and inspection plan is also submitted annually to this committee for validation. This committee is informed every six months of the results of the follow-up recommendations of internal audit, inspection, oversight bodies and statutory auditors and of the progress made in related action plans. Regular reports of activity are also presented for study. In addition, the annual report on internal control at SFIL and Caisse Française de Financement Local (articles 258 and following of the *arrêté* of November 3, 2014) is presented every year for review. A synthesis of these different reports is presented to SFIL's Board of Directors by the Chairman of the Risks and Internal Control Committee and to the Executive Board and the Supervisory Board of Caisse Française de Financement Local.

8.1.7. Specific Controller

The Specific Controller of Caisse Française de Financement Local is a French professionally certified auditor named by the Company's Supervisory Board. The Specific Controller carries out controls pursuant to articles L.513-23 and L.513-24 and articles R.513-15 and R.513-16 of the Monetary and Financial Code as well as CRBF standard 99-10. He is responsible for ensuring that the Company respects its exclusive corporate purpose and prudential standards. He conducts appropriate audits in cooperation with the statutory auditors and is completely independent vis-à-vis the Company's officers. He is also liable for the negative consequences of any error or negligence committed in the exercise of his functions. The Specific Controller has access to all information from management, internal control units and internal audit. In addition, operating services and internal control units have been instructed to provide specified information in order to allow the Specific Controller to monitor the over-collateralization ratio, the nature of assets, interest rate risk management, the gap in the average life of assets and privileged liabilities, coverage of cash needs over 180 days, and the coverage plan of privileged liabilities by the assets. For every Caisse Française de Financement Local issue contract or on the basis of a quarterly issuance program, he affirms compliance with legal and regulatory standards concerning the over-collateralization ratio of the privileged liabilities by the assets, once the issue has been settled. The Specific Controller certifies that the documents the Company sends to the ACPR meet legal and regulatory requirements for *sociétés de crédit foncier*. At the request of the Banque de France, the Specific Controller annually issues a certificate in support of the statement submitted by Caisse Française de Financement Local concerning the composition of the cover pool. He submits an annual report on his activity to the Supervisory Board of Caisse Française de Financement Local, and a copy is addressed to the Autorité de contrôle prudentiel et de résolution (ACPR).

8.2. PREPARATION OF ACCOUNTING AND FINANCIAL INFORMATION

8.2.1. Financial statements

A company's annual financial statements, in addition to all the financial data produced by the Accounting department should give a true and fair view of its assets, financial position and results. For credit institutions, the *arrêté* of November 3, 2014, on internal control highlights in its accounting chapter that the organization adopted should guarantee the existence of procedures called audit tracks. They make it possible to establish a link between accounting data and the original justification, and vice-versa. All these items should make it possible to reconstitute, justify and explain any and all financial items produced for accounting or regulatory purposes. This principle grounds the organization of accounting practices in the SFIL Group and also applies to both SFIL and Caisse Française de Financement Local.

In 2017, attention focused on preparing for changes resulting from the introduction of new accounting standards applicable from 2018, in particular preparing for the implementation of IFRS 9, the expected impacts of which are set out in detail in the notes to the financial statements and in the management report. The accounting teams also contributed significantly to the work carried out on the Group's information system, of which a number of components are being overhauled in 2017 and 2018.

8.2.1.1. Role and organization of Accounting

Accounting data is produced at Caisse Française de Financement Local by the Accounting division of SFIL, within the framework of the management agreement between the two companies. Accounting at SFIL reports to the Chief Financial Officer (CFO), who also oversees the Back-Office and Financial Performance Management divisions, including the oversight of balance sheets, management control and purchasing. Accounting plays a central role in the piloting of SFIL and in financial management, thereby making it possible to benefit from this central viewpoint.

Accounting produces basic accounting data for the financial statements of Caisse Française de Financement Local. It also provides accounting data for La Banque Postale within the framework of the business at hand. It is also responsible for producing the consolidated financial statements of the SFIL Group and, with the Risks division, ensuring all regulatory and prudential standards are respected.

Accounting has a role of analysis and verification of accounting data. It relies on the reconciliation of a set of figures with that of other teams in Finance. This approach is used to analyze the income, but also to confirm the information on the Company's balance sheet, and in particular entries to risk bases used to calculate prudential indicators.

To carry out its mission, Accounting gets all the information required in participating in committees either directly or through the Chief Financial Officer. It participates in the development of IT systems, and relies on a cross-division team within the Strategic IT Project division to improve, secure and ensure long life to its IT system. In particular, this division is in charge of accounting and regulatory tools as well as ALM and management control tools. It has the mission to participate actively in the development and the improvement of the tools used by SFIL's operating divisions. This system makes it possible to ensure continuous improvement in terms of quality, process efficiency and the reliability of financial information.

8.2.1.2. Preparation of the financial statements

In the preparation of the financial statements, the accounting system of Caisse Française de Financement Local is in large measure automatically supplied by upstream management systems that manage transactions with customers and market counterparties as well as operating expenses. When data is entered into one of the management systems, it is automatically recorded in accounting according to a pre-defined plan, and complemented by manual entries for certain types of operations. Caisse Française de Financement Local can record operations in a single accounting system based on a double

set of accounting standards (French GAAP and EU IFRS). The synthesis of this data is thus obtained automatically using parameterized publication tools.

The internal control system in the operating divisions guarantees the completeness and accuracy of accounting entries. The team in charge of accounting standards ensures compliance with standards, validates automated accounting procedures and examines complex or unusual operations. When certain operations can not be completely incorporated into the management tools available, they are processed using specific internal control procedures.

A first level of control is conducted by Accounting teams that are specialized by products, in particular by analyzing accounting/management data reconciliation, bank reconciliation and technical suspense accounts. Monthly comparisons with management data and reconciliations of micro-hedges make it possible to ensure the correct transcription of financial operations. In order to verify the coherence of interest expense and income from one period to another, this data is compared with average outstandings in order to produce average rates that are easier to compare from one period to the next. Finally, these teams also prepare a synthetic memorandum on the work done which points out areas that need attention and improvement for the processes to be used in future financial statements.

Complementary controls are carried out by other teams from Accounting at the monthly, quarterly and annual closings. Through specific reviews, the teams in charge of preparing the financial statements check the quality of the work done by the teams responsible for first-level control. These teams also reconcile the accounting data from Net banking income with management data produced by separate teams. This cross referencing is done at least once a quarter and consistency from one period to the next is verified using analytical controls. The main changes deserve an explanation. These analyses are synthesized in a quarterly report that is submitted to the Chairman of the Executive Board of Caisse Française de Financement Local.

To ensure thorough implementation of its control plan, Accounting has a monitoring tool at its disposal with which it can verify the deployment of key controls and their validation. This information and any comments on discrepancies are subject to review by the head of Accounting with the main team members.

The preparation of the financial statements is carried out by the aggregation of the accounts thus produced according to an automated and standardized process. This function requires parameters administered by a dedicated and independent team. Stability in reporting, which represents a key point in terms of communication, is thereby verified. Notes to the consolidated and financial statements are generally produced based on accounting data that may be enhanced by management information. Qualitative analyses are then carried out through cross-referenced controls of synthetic data in accounting as well as with the contribution of the teams in charge of monitoring the Group's balance sheet. Cross-referenced controls are also conducted between the financial statements and the notes to the financial statements. Throughout this process, reviews and controls are carried out according to the hierarchical delegations that exist.

8.2.1.3. Approval of the financial statements

The financial statements, balance sheet, income statement and notes are subject to particular scrutiny during the preparatory phase and in their final form by a delegated member of Caisse Française de Financement Local's Executive Board. The Executive Board of Caisse Française de Financement Local approves the yearly and half-yearly financial statements at a meeting attended by the two statutory auditors and the accounting department. The principal issues in the period's management report are also examined on this occasion. These annual and half-year financial statements are subject to an audit and a review (respectively) by the statutory auditors.

The annual financial report is prepared by Caisse Française de Financement Local's Executive Board in liaison with units of SFIL, in particular the CAFFIL Coordination division, Accounting, Risks and the General Secretary. The Company's statutory auditors verify the information it contains. This document is presented to Caisse Française de Financement Local's Supervisory Board, and then to the annual shareholders' meeting.

The calling of shareholders' meetings and the right to attend such meetings are described in articles 27 and 28 of the Company's by-laws.

8.2.1.4. Publication of the financial statements of Caisse Française de Financement Local

This accounting and financial information is made public in several ways. In addition to the regulatory publication in the BALO, the half-year and annual financial statements, together with the corresponding management reports, are posted on the Internet site www.caffil.fr and www.caissefrancaisedefinancementlocal.fr. Half-year and annual financial reports are posted on the Autorité des Marchés Financiers (AMF) through the NASDAQ regulatory information wire. Moreover, unaudited activity reports are drawn up to describe the situation as of March 31 and September 30. They are available to the public on the Company's Website.

Some of this information is also available, with differences in presentation, in the report on the quality of the assets that is submitted to regulatory authorities and posted on the Internet site of Caisse Française de Financement Local, in compliance with CRBF instruction 2011-I-07. Other information is also posted on the Website of the Company, as required by the Covered Bond Label.

8.2.1.5. Role of statutory auditors

Both SFIL and Caisse Française de Financement Local are audited by two auditing firms working together.

The statutory auditors review the financial statements only on a yearly and half-yearly basis. They are consulted throughout the process of preparation of the financial statements in order to ensure efficiency and transparency. In due diligence, they analyze accounting procedures and evaluate current internal control systems to determine the nature, period and extent of

their controls of the principal areas of risk. They may make recommendations on internal control procedures and systems that could improve the quality of financial and accounting information produced. They have access to all memoranda and notes produced by staff that is in charge of accounting principles and standards, and they also review the accounting manuals, as well as the analyses conducted by the Accounting teams. They consult internal audit and inspection reports. They verify the consistency of the data in the management report with the accounting information, as well as the conformity of the management report and the financial statements with all the items they have reviewed and audited. Their contribution includes a review of all the agreements that are regulated. They provide an exhaustive and accurate summary of regulated agreements in the special report they submit at the end of their annual mission. They employ due diligence to obtain reasonable assurance that the financial statements are free of any material misstatement.

8.2.2. Management reporting

The financial statements (balance sheet, off-balance sheet, income statement, cash flow statement and notes) that Caisse Française de Financement Local communicates to its shareholder and to the general public are completed by quarterly activity reports.

This management information also includes items related to loans originated by La Banque Postale and acquired by Caisse Française de Financement Local, as well as to the refinancing of large export credits and updates on the reduction of the sensitivity of structured loans. This data is accompanied by forecasts and evaluations of risks, which is directly supplied by the operating divisions or the Risks division before it is incorporated into the annual financial report. Their accuracy is therefore guaranteed by the internal control system of the divisions concerned.

New loans are granted solely in France as concerns LBP's marketing activity, as well as the business of refinancing large export credits and the efforts to reduce the sensitivity of structured loans. A geographic breakdown of borrowers who are French residents and those who are domiciled in another country is presented in the Management Report. This data is prepared by the Financial Performance Management division based on management and accounting data.

Since, at the same time, SFIL manages Caisse Française de Financement Local and acts as servicer for La Banque Postale, analytical accounting of costs has been adopted to ensure proper billing of financial services rendered.

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9. Risks management

9.1 - OVERVIEW OF THE RISK MANAGEMENT SYSTEM

Because the Company is an issuer of covered bonds, the risks authorized for Caisse Française de Financement Local are strictly selected and limited. When the Company was created, a distinction was made between risks that are compatible and risks that are not compatible with the legal and regulatory framework of *sociétés de crédit foncier* and with the specific nature of Caisse Française de Financement Local's by-laws and its license granted by the Comité des établissements de crédit et des entreprises d'investissement (CECEI), now merged into the Autorité de contrôle prudentiel et de résolution (ACPR).

The criteria of the rating agencies define restrictions or limits for risks compatible with the Company's activity.

The general approach decided by the Executive Board of Caisse Française de Financement Local and applied in every unit of SFIL in charge of the operations concerned involves monitoring that:

- risks not compatible with the activity of Caisse Française de Financement Local are not taken by the Company or are eliminated from the start;
- risks compatible with the activity are maintained exactly within authorized limits;
- controls are defined by the Risks division and carried out by the front and middle offices of SFIL. The results of the controls are reported to the Executive Board of Caisse Française de Financement Local and any anomalies discovered during such controls are reported to the Supervisory Board. Finally, these results are transmitted to the Specific Controller and the data is made available for his review.

SFIL and Caisse Française de Financement Local have implemented a complete risk management system:

- to identify, monitor, manage and measure risks using specific methods;
- to decide on limits to be implemented;
- to decide on delegations to assign to the front office teams;
- to decide on the amount of provisions that are required;
- to inform the competent committees regarding changes in these risks, proactively warning them that a limit or threshold has been exceeded.

The level of risk that is acceptable for SFIL and Caisse Française de Financement Local is defined by Executive Management and the Risks Committee at SFIL, in line with the risk appetite of the two companies. It is then approved by the SFIL Risks and Internal Control Committee and finally by the SFIL Board of Directors. It is also approved by the Executive and Supervisory Boards of Caisse Française de Financement Local. Within this framework, policies have been defined for the entire scope as well as limits and rules for delegating decisions. The Risk Management division monitors these limits and, where appropriate, proposes measures to Executive Management to ensure compliance therewith.

A Quarterly Risks Review is presented to the Risks and Internal Control Committee every quarter by the head of risks of SFIL. This review provides a synthetic view of the main risks at SFIL and Caisse Française de Financement Local and their development during the quarter (credit risks, market and balance sheet risks, operational risks) as well as changes in regu-

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lations over the period. Items concerning Caisse Française de Financement Local are also presented by the Executive Board to the Supervisory Board of Caisse Française de Financement Local.

All operations conducted by Caisse Française de Financement Local are subject to the control by different committees set up by SFIL. This oversight takes into account the particular rules and limits applicable to Caisse Française de Financement Local.

The Risks division relies on several committees, the missions and composition of which have been approved by the Risks and Internal Control Committee of SFIL. These committees may be cross-divisional – Risks Committee, Committee on the Validation of Methods and Models, New Products Committee – or specialized on credit risks, market risks and operational risks.

The Risks Committee defines the risk profile of SFIL and Caisse Française de Financement Local, validates risk control dispositions and ensures their respect. In particular, it is in charge of defining delegations in the granting of credit and approving the risk policies of SFIL concerning all types of risks and the limits defined by the Risks division.

The Market Validation Committee is responsible for validating and implementing the Group's market risk and derivatives valuation models. The Credit Validation and Quality Control Committee is responsible for validating the internal rating systems used to calculate regulatory capital and the IFRS 9 impairment and economic capital models as well as their implementation.

The New Products Committee, chaired by the SFIL's Chief Risks Officer, examines all new products, management processes and transformation of a pre-existing product or process. It makes decisions in this respect. This committee also studies new products intended for financing, refinancing or hedging risks, as well as the development of any existing product or service to the extent that it substantially modifies the risk profile or the internal processes of the Company. It also determines and evaluates the risks of non-compliance connected to the creation or modifications of products or services based on the compliance opinion submitted to it.

9.2 – CAISSE FRANCAISE DE FINANCEMENT LOCAL'S MAIN RISKS

9.2.1. Credit Risk

9.2.1.1. Definition

Credit risk represents the potential loss that Caisse Française de Financement Local may incur as the result of the decline in a counterparty's solvency.

9.2.1.2. Organization and governance

The Risks division defines the policies, guidelines and procedures relating to credit risk. It is responsible for developing the decision-making process (principally the granting of loans) and the framework of delegations and for supervising the analysis and rating process. SFIL's Risks Committee and Caisse Française de Financement Local's Executive Board are responsible for final approval of the credit risk policies.

Within the framework of its surveillance of credit risk, the Risks division provides for:

- the definition of credit risk policies in conformity with the risk appetite of SFIL and Caisse Française de Financement Local;
- the definition of limits by type of counterparty setting the maximum exposure considered to be acceptable;
- the proactive monitoring of limits, which the Risks division may change at any time in function of trends in related risks;
- the definition of delegations by type of counterparty and the monitoring of respect for the rules governing the lending process;
- the management of the lending process both for new commitments and rescheduled loans through credit analyses and internal ratings (by using either the internal rating systems or expert advice);
- the monitoring of credit risk in all the portfolios of SFIL and Caisse Française de Financement Local (local public sector in France, international, bank counterparty, export credit, etc.) by generating credit analyses and reviewing ratings annually;
- the identification of assets with downgraded risks susceptible to be put on the watchlist;
- the proposal of specific or segment-based impairment for the portfolio.

The Risks division is also in charge of maintaining and developing:

- internal rating systems for the French and Italian local public sector, for banks and sovereign;
- Pillar 2 models (economic capital).

The Risks division finally deals with statistical models linked to the different stress scenarios.

The Risks division relies on several specialized committees, as described below.

- The Credit Committee approves new commitments⁽¹⁾ by SFIL and Caisse Française de Financement Local (loans and market transactions) and the rescheduled loan agreements on the balance sheet of Caisse Française de Financement Local. It sets credit limits when certain predefined thresholds are exceeded. Each file presented to the Credit Committee contains

(1) Except for commitments delegated to the Risks division, to the Debt Portfolio Management division, and the sales teams of La Banque Postale.

an independent analysis conducted by the Risks division. At each meeting, the Credit Committee is also informed of commitments made within the framework of delegations granted to the Risks division, to the Debt Portfolio Management division, the Treasury and Financial Markets division or the commercial teams of La Banque Postale. This committee meets on a weekly basis.

- The Watchlist Committee is in charge of monitoring assets kept under particular scrutiny because of the downgrade of risk and it may propose specific impairment. This committee meets quarterly.
- The Default Committee decides whether a file should be given default status or be upgraded, and it qualifies debt due as real default, operational debt due or technical debt due. This committee meets quarterly.
- Every quarter, the Impairment Committee sets the amount of collective impairment and finalizes the calculation of specific impairment on the basis of the provision rate decided by the Watchlist Committee.
- The Non-Performing Exposures and Forbearance Committee quarterly approves the list of counterparties with non-performing exposures and a second list for counterparties that benefited from financial concessions due to their financial difficulties.
- The Rating Committee ensures the proper application of the internal rating systems and the appropriateness of the rating processes. This committee meets quarterly. Although it is an integral part of the credit risk management process, the committee is organized by the head of the Validation Credit and Quality Control team, which reports directly to the head of Risks in order to guarantee the independence of the control process.

Moreover, within the framework of the purchase of assets by Caisse Française de Financement Local, the control of eligibility is organized at two successive levels.

- The CAFFIL Coordination division within SFIL pilots the process of asset acquisition and associated controls of eligibility prepared by the different divisions of SFIL; the definitive portfolio is validated by the Executive Board after soliciting the opinion of the SFIL's Credit Committee.
- The customer back-office division carries out permanent controls daily on outstanding assets.

These controls are standardized by procedures.

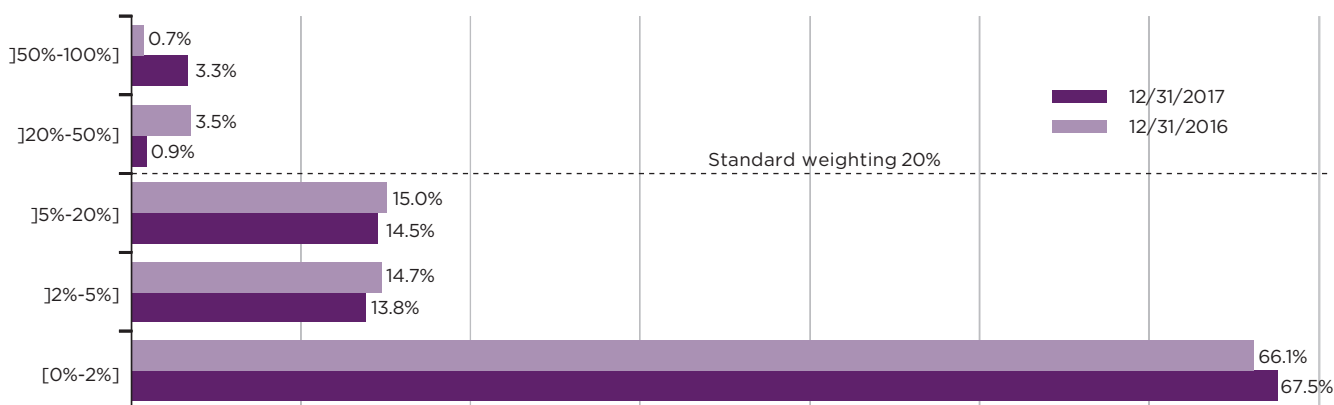
The Specific Controller also carries out regular, detailed ex-post checks on asset eligibility.

9.2.1.3. Breakdown of exposures according to risk weighting

The quality of Caisse Française de Financement Local's portfolio is illustrated by the risk weighting assigned to its assets (Risk Weighted Assets) for the calculation of the bank's solvency ratio. This reflects the fact that for most of its assets SFIL has opted for the advanced method of calculating regulatory capital requirements. Banking regulators authorized the Company to use the advanced internal models developed for the consolidated calculation and reporting of capital requirements for credit risk. The calculation of such weighting in particular combines the probability of default (PD) and loss given default (LGD) of the counterparty.

This enables Caisse Française de Financement Local to present an analysis of its exposure as of December 31, 2017, broken down by risk weighting, such as used for the calculation of capital requirements for credit risk.

Risk weighting of Caisse Française de Financement Local's portfolio as of December 31, 2017



This analysis confirms the excellent quality of the assets in Caisse Française de Financement Local's portfolio:

- more than 81% of the portfolio has a weighting of less than 5%;
- the average risk weighting of the cover pool assets is 6.6%, versus 20% for European local governments according to the Basel II/III standard method;
- only 4% of the portfolio has a weighting of more than 20%.

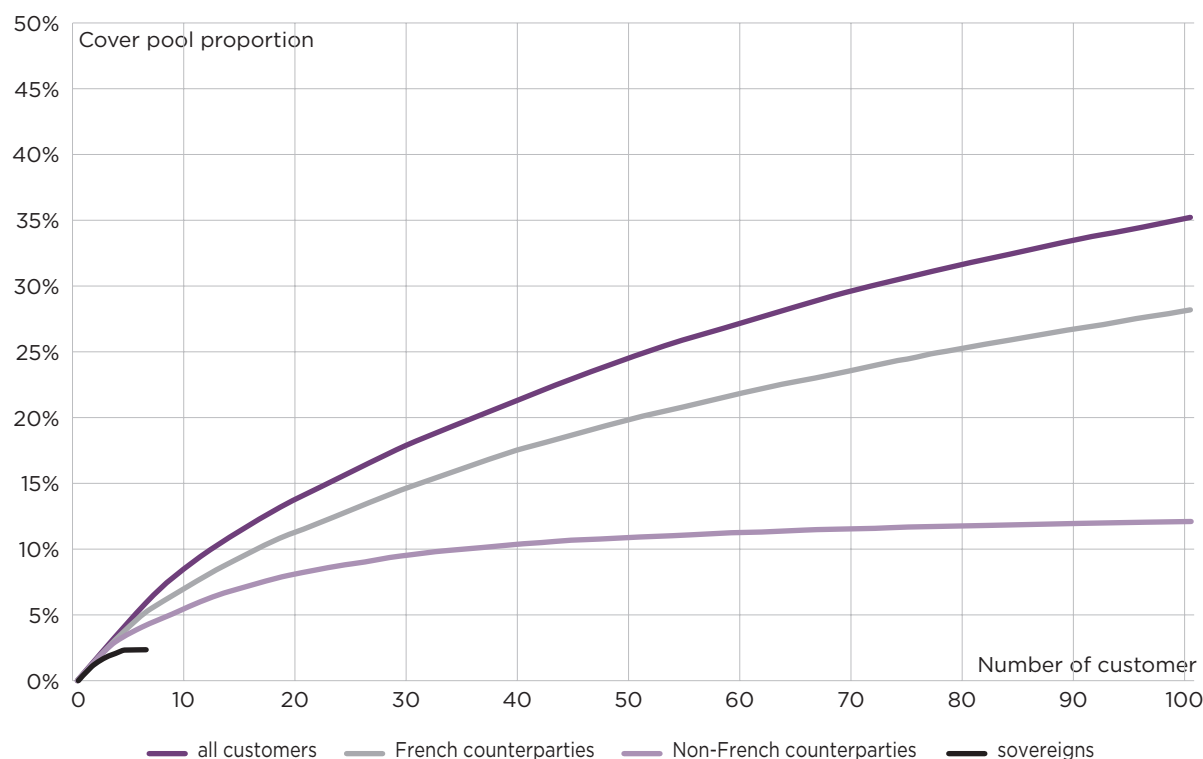
Weighted exposure with respect to credit risk amounted to EUR 4,864 million. Including weighted assets associated with the credit valuation adjustment (CVA) volatility risk and with operational risk (there being no risk weighted assets associated with market risk), total risk weighted assets came to EUR 5,508 million. Combined with its high level of regulatory equity, the credit quality of Caisse Française de Financement Local's assets enabled the Company to post a phased-in Basel III solvency ratio of 24.0% as of December 31, 2017. The fully loaded Common Equity Tier 1 Ratio in Basel III was 23.2% as of December 31, 2017.

9.2.1.4. Concentration by customer

The risk of concentration refers to exposure to a limited number of counterparties. Diversification can make it possible to avoid this problem, and it is a risk management tool to protect from any loss in capital.

The chart below presents the concentration of cover pool by type of counterparty. It confirms the great diversity of Caisse Française de Financement Local's portfolio of assets.

Cover pool concentration by type of customer



As of December 31, 2017, all categories combined, the 20 largest exposures (excluding replacement assets and cash investments) represented 14% of the global cover pool (stable compared with December 31, 2016). The largest exposure accounted for only 1.1% of the cover pool and the twentieth exposure 0.5%.

9.2.1.5. Non-performing loans, litigious loans, provisions

Caisse Française de Financement Local's loans and most of its securities are classified in the Loans and receivables portfolio under IFRS, reflecting its intention to hold them until maturity. They are measured at amortized cost, plus, for fair value hedges, any changes in the fair value of hedged risk ; they are subject, if appropriate, to impairment provisions if they show a non-recovery risk.

In addition, collective provisions are calculated on the various loans and receivables portfolios. In the absence of specific impairment, they cover the impairment risk relating to objective indications of probable losses on certain portfolio segments or other lending commitments in force at the closing date. These losses are estimated on the basis of experience and each segment's past performance, as well as the borrowers' ratings and current economic environment. For this purpose, Caisse Française de Financement Local uses a credit risk model based on historical losses, which uses an approach combining probability of default and loss given default. This model is regularly tested, on an ex-post basis.

As of December 31, 2017, arrears amounted to EUR 65 million, representing a decrease of 20% from December 31, 2016 (EUR 81 million) and 51% from December 31, 2015. Arrears are concentrated on a very limited number of counterparties.

As of December 31, 2017, non-performing and litigious loans represented 1% (EUR 558 million) of Caisse Française de Financement Local's cover pool, illustrating the portfolio's excellent quality. They were stable compared with December 31, 2016 (EUR 557 million) and down 17% compared with December 31, 2015 (EUR 673 million).

EUR millions	12/31/2015	12/31/2016	12/31/2017
Non-performing loans and litigious loans	673	557	558
% of cover pool	1.1%	1.0%	1.0%
Arrears	133	81	65

Non-performing and litigious loans comprise:

- EUR 526 million of receivables classified as non-performing, corresponding to loans granted to customers whose total unpaid outstanding came to EUR 33 million (including EUR 28 million on structured loans). When a customer is classified in default in terms of credit risk, the outstanding amount of all its loans is automatically classified as non-performing, by contagion, in addition to its existing past dues;

- EUR 32 million in receivables classified as litigious, corresponding to unpaid interest on structured loans subject to ongoing legal proceedings.

The table below shows the breakdown of non-performing and litigious loans by type of borrowers.

Non-performing and litigious loans EUR millions	12/31/2016		12/31/2017	
	Non-performing loans	Litigious loans	Non-performing loans	Litigious loans
FRANCE				
State	-	-	-	-
Regions	54	-	52	-
Departments	70	-	-	23
Groups of municipalities	117	14	118	-
Municipalities	268	12	238	8
Public sector entities	21	1	118	1
TOTAL NON-PERFORMING AND LITIGIOUS	530	27	526	32
<i>of which arrears on structured loans</i>	<i>46</i>	<i>27</i>	<i>28</i>	<i>32</i>
<i>of which arrears on other loans</i>	<i>8</i>	<i>-</i>	<i>5</i>	<i>-</i>

The table below shows the change in the number of non-performing customers and customers with a portion of their outstanding loans classified as litigious (past dues on sensitive loans).

Non-performing loans and litigious loans (number of customers)	2016		2017	
	Non-performing loans	Litigious loans	Non-performing loans	Litigious loans
BEGINNING OF THE YEAR	74	35	49	14
New	17	4	29	1
Outgoing	42	25	17	8
END OF THE YEAR	49	14	61	7

The number of customers classified as litigious decreased significantly in 2017. At the same time, the number of customers classified as non-performing increased owing to:

- the transfer of customers initially considered to be litigious on account of their structured loans;
- the inclusion in this category of customers with a very low level of past dues on non-structured loans.

The table below shows the total amount of provisions as of December 31, 2017 pursuant to IFRS.

EUR millions	12/31/2016	12/31/2017
Specific impairment	60	23
Collective impairment	46	30
TOTAL	106	53

As of December 31, 2017, specific impairments under IFRS amounted to EUR 23 million. The change in this amount compared with December 31, 2016 takes into account a reversal in 2017 following the use of more accurate method for estimating recoverable flows on non-performing loans⁽¹⁾.

In addition, collective impairments are calculated on the various loans and receivables portfolios. These provisions amounted to EUR 30 million at end-2017 compared with EUR 46 million at end-2016. The review of the loan portfolios and associated risks led to an adjustment reversing collective impairments in a total amount of EUR 16 million, reflecting notably progress in reducing sensitive loans, which made it possible to reassess the legal risk associated with customers who have taken out legal action against Caisse Française de Financement Local.

As a result, at the end of 2017, the Cost of risk calculated in accordance with IFRS showed an improvement of EUR 53 million.

9.2.1.6. Bank counterparty risk

Counterparty risk refers to the risk of loss on an exposure linked to the default of a counterparty. It is naturally in function of the amount of the exposure, the probability of default on the part of the counterparty, and the portion of the loan that cannot be recovered in the event of default.

Caisse Française de Financement Local holds three types of exposure to banks:

- replacement assets in the amount of EUR 0.9 billion (see 4.2.2.);
- bank account balances in euros and other currencies, representing EUR 10 million, excluding cash deposited on the Banque de France account;

⁽¹⁾ Within the framework of the successful policy to reduce the interest rate sensitivity in 2016 and the confirmation of legal decisions favorable to the bank, Caisse Française de Financement Local was able to hone, in a reasonable and prudent manner, the methods it uses to estimate the recoverability of flows of non-performing loans on its balance sheet. In particular, in order to account for the impact of the spread of payments, the implementation of this approach, which is in compliance with IFRS, makes it no longer systematically necessary to estimate the total amount of interest to account for hypotheses of future recovery. Thus, the net interest rate expense is improved through a recovery of provisions in the amount of EUR 31 million, recorded as of December 31, 2017.

- its derivative contracts, entered into within the framework of its management of interest rate and foreign exchange risks.

All of Caisse Française de Financement Local's derivative operations are conducted within the framework of standard ISDA or FBF (Fédération bancaire française) contracts with major international banks. These contracts have particular characteristics, since they must meet the standards set by rating agencies for *sociétés de crédit foncier* (and other issuers of covered bonds). In 2017, Caisse Française de Financement Local amended these contracts to take into account recent regulatory changes (variation margin amendments). These interest rate and currency swaps all benefit from the same legal privilege as *obligations foncières*. For this reason, Caisse Française de Financement Local does not pay its derivative counterparties any collateral (or variation margin), whereas they have to pay Caisse Française de Financement Local except for some which benefit from the agencies' highest short-term rating.

At the end of December 2017, Caisse Française de Financement Local was exposed (positive fair value of the swaps) on nine banking counterparties, eight of these paid cash collateral of EUR 0.7 billion, offsetting total exposure, and one paid no collateral because of its very good short-term rating. This counterparty represented a limited exposure (EUR 8 million).

All derivative exposures as of December 31, 2017, are listed below.

EUR billions	Short-term notional amounts	Long-term notional amounts	% of long-term notional amounts	Mark to market		Collateral received	Number of counterparties
				-	+		
SFIL	-	15.4	18.7%	(1.6)	-	-	1
Other counterparties	46.8	66.7	81.3%	(2.4)	0.7	0.7	25
TOTAL	46.8	82.1	100.0%	(4.0)	0.7	0.7	26

The swaps negotiated with external counterparties represented 81.3% of outstanding long-term swaps and those signed with SFIL 18.7%. The long-term swaps signed with the five largest counterparties represented a total of 44% of notional amounts.

Short-term swaps (Eonia) were all contracted with external counterparties.

9.2.2. Market risk

9.2.2.1. Definition

Market risk is defined as the potential risk of loss (through income statement or directly through other comprehensive income) resulting from fluctuations in the prices of financial instruments that make up a particular portfolio. If the transactions of a portfolio are entered into for trading purposes, regulatory market risk requires daily monitoring of risks and results indicators of that portfolio. Changes in the value of trading portfolios directly impact the income statement.

Caisse Française de Financement Local, as a *société de crédit foncier*, is not authorized to hold a trading or stocks investment portfolio and is therefore not exposed to regulatory market risk.

Caisse Française de Financement Local's banking portfolio positions and activities that pose a risk to its accounting income and equity as a result of exposure to market volatility are monitored as non-regulatory market risks. These are mainly market risks resulting from fluctuation of the available for sale (AFS) reserve or the provision for placement securities under French GAAP, as well as risks resulting from the export credit activity (monitoring of the value changes of the indicator specific to export credit and, for USD-denominated loans, the change in the valuation of currency swaps hedging this activity). Changes in accounting valuation adjustments on derivatives, such as credit valuation adjustments (CVA), debit valuation adjustments (DVA) and funding valuation adjustments (FVA) are also considered as non-regulatory market risks.

9.2.2.2. Governance

The governance of market risks is built around the Market Risks Committee, which conducts a quarterly review of defined risk indicators (sensitivity, mark to market changes in structured swaps hedging the assets of customers in default, and monitoring of AFS reserves, provisions for placement securities under French GAAP, limits, cash collateral received and export credit activity indicators). This committee is also in charge of approving the policies, guidelines and procedures relating to market risks for submission to the Risks Committee.

The continuous monitoring of non-regulatory market risks is carried out by SFIL's Market and Balance Sheet Risks division, which is mainly responsible for:

- defining policies, guidelines and procedures related to the monitoring of market risks;
- defining limits;
- defining calculation and assessment methods for these risks;
- validating the valuation of derivatives for accounting purposes;
- carrying out daily controls of margin calls on derivatives (cash collateral);
- valuing balance sheet items (assets and liabilities);
- monitoring the valuation of currency swaps entered into to hedge refinancing loans for large export credits in USD not yet recognized under hedge accounting;
- monitoring the valuation of swaps that can no longer be classified under hedge accounting following the default of certain customers.

Control of non-regulatory market risks is carried out by monitoring sensitivity to market variables (the «Greeks»), which reflects instruments' fair value change in response to a standardized movement (or shock) in market variables.

The interest rate risk on securities not offering a variable rate at outset that are classified as AFS or placement securities under French GAAP is generally hedged by swaps. The securities portfolio's residual risk is therefore limited to its credit spread risk. The Market and Balance Sheet Risks division calculates the AFS reserve's sensitivity to issuers' credit spreads.

It also monitors accounting valuation adjustments on derivatives (CVA, DVA and FVA) every quarter.

9.2.3. ALM risk

9.2.3.1. Governance

Balance sheet risk management is structured around three committees:

- the Asset-Liability Management (ALM) Committee, on which sit representatives of the Finance division's ALM unit, the Market and Balance Sheet Risks division and the other bank business lines concerned by this management, determines the strategy for managing balance sheet risks and ensures that it is correctly applied by monitoring management indicators;
- the Interest Rate ALM and Liquidity ALM committees prepare information for the ALM Committee and are responsible for implementing its decisions operationally.

The Finance division's ALM unit is responsible for implementing the ALM policies defined for SFIL and Caisse Française de Financement Local in compliance with the relevant management limits and regulatory framework.

The Market and Balance Sheet Risks division is in charge of defining the balance sheet risk management policy, calibrating and monitoring the limits on ALM indicators and performing second-level controls on most of these indicators.

9.2.3.2. Liquidity risk

Definition

Liquidity risk is defined as the risk that the institution may not be able to find the necessary liquidity, on a timely basis and at a reasonable cost, to cover the financing needs related to its activity.

Liquidity risk management

Caisse Française de Financement Local's liquidity risk mainly reflects how able it is to reimburse certain debts benefiting from the legal privilege on a timely basis in the event of an excessive lag between the repayment of its assets and that of its debt benefiting from the legal privilege. It relates to the fact that SFIL is responsible for most of the funding requirement associated with the Caisse Française de Financement Local's over-collateralization⁽¹⁾.

Caisse Française de Financement Local has two main types of liquidity need:

- financing of the assets (EUR 46.9 billion in loans, EUR 7.2 billion in securities, and EUR 1.7 billion in cash deposited with the Banque de France) that cover the *obligations foncières* it issues;
- financing of the liquidity requirements related to compliance with regulatory ratios, specific *sociétés de crédit foncier* ratios and the rating agency methodologies used to meet a rating target.

The sources of financing used to meet these requirements, other than the entity's equity (EUR 1.5 billion), are:

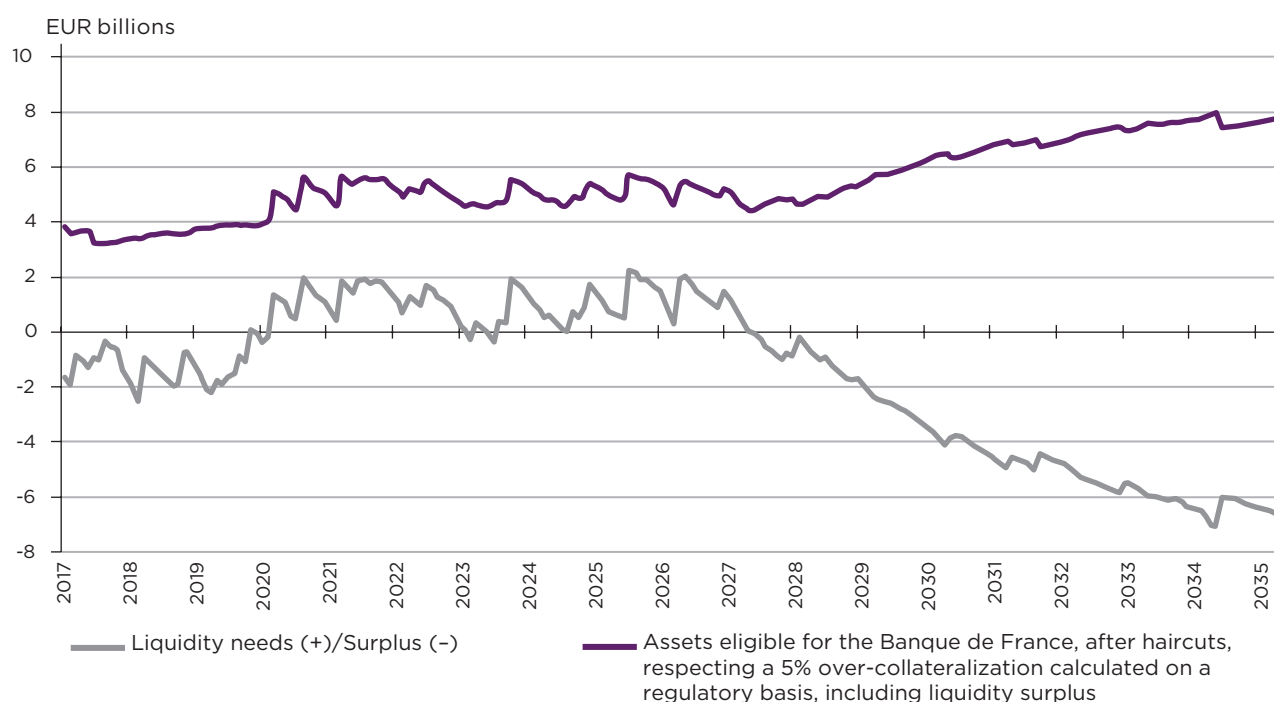
- debt benefiting from the legal privilege, i.e. *obligations foncières* and registered covered bonds (EUR 49.0 billion) and the cash collateral received by Caisse Française de Financement Local (EUR 0.7 billion);
- refinancing arising from the loan agreement entered into with SFIL to cover the financing requirements related to Caisse Française de Financement Local's over-collateralization (EUR 4.8 billion).

Furthermore, Caisse Française de Financement Local has a large stock of assets eligible for European Central Bank refinancing via the Banque de France. In addition to access to the central bank in its own name, Caisse Française de Financement Local can also mobilize certain of its assets by using interbank financing in the form of repurchase agreements. If necessary, these transactions would easily cover its cash flow requirements. There were no transactions of this type in 2017, except for operational tests.

The aggregate maximum liquidity requirement that Caisse Française de Financement Local could face in the future in a run-off situation in which it was unable to issue new *obligations foncières* is lower than the maximum funding already occasionally obtained on a one-off basis from the central bank in the past. It is also lower than the Caisse Française de Financement Local's refinancing potential with the Banque de France, measured by the amount of eligible assets after haircut that would be available while complying with the minimum over-collateralization required by the regulations.

The chart below shows the forecast aggregate liquidity requirement and the assets needed to cover this requirement.

(1) A part of Caisse Française de Financement Local's over-collateralization is refinanced by its equity.

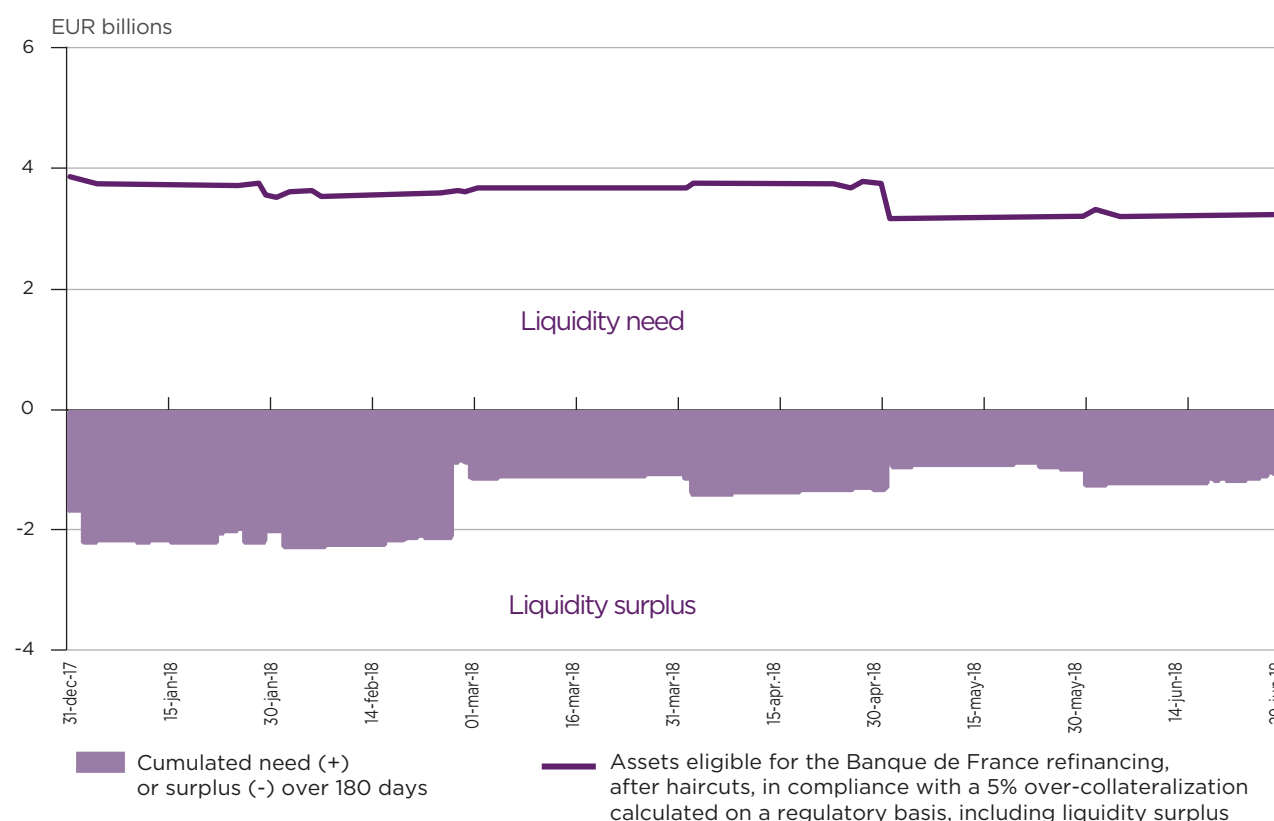


Caisse Française de Financement Local has its own autonomous resources that enable it to cover its temporary liquidity needs, even in the event of the default of its parent company, since any legal proceedings engaged for the bankruptcy or liquidation of its parent company cannot be extended to Caisse Française de Financement Local (article L.513-20 of the Monetary and Financial Code).

Meanwhile, Caisse Française de Financement Local manages its liquidity risk using the following indicators:

• Regulatory indicators specific to *sociétés de crédit foncier*:

- the regulatory coverage ratio (or over-collateralization ratio): this represents the ratio between assets and debts benefiting from the legal privilege, and must be at least 105% (see section 6.);
- the maximum gap of 1.5 years between the average maturity of debt benefiting from the legal privilege and that of assets eligible to make up the minimum amount necessary to meet the regulatory coverage ratio (see the specific section on transformation risk below).
- forecast cash needs at 180 days: Caisse Française de Financement Local ensures that, at any times, its cash needs over a period of 180 days are covered by replacement assets and assets eligible for Banque de France's credit operations. Cash needs include repayments of *obligations foncières* and registered covered bonds, debt not benefiting from the legal privilege and forecast repayments of cash collateral received, after deduction of cash flows from amortization of assets. This forecast is published quarterly in the Asset Quality Report, and is shown below. At the end of December 2017, there was a liquidity surplus for the whole period.



- The regulatory liquidity indicators applicable to credit institutions, in particular the liquidity coverage ratio (LCR). As of 31 December, 2017, Caisse Française de Financement Local's LCR was 371%.
- Internal liquidity indicators:
 - the liquidity projections for the short term (three months) and long term (two years);
 - the management coverage ratio (or over-collateralization ratio), which targets an over-collateralization level consistent with the Caisse Française de Financement Local's target rating (see section 6.);
 - the difference in duration between assets and debts benefiting from the legal privilege (limited to three years): this is published every quarter and came to 0.95 years as of December 31, 2017 (see the specific section on transformation risk below);
 - the maximum difference between assets and liabilities maturing within the same year, this limit being reviewed annually;
 - the one-year survival horizon in stressed conditions;
 - the sensitivity of the net present value of the static liquidity gap adjusted for regulatory constraints (compliance with the LCR and the over-collateralization ratio);
 - the indicators related to refinancing of large export credits activity: consumption of the spread and EUR/USD basis risk appetite by the various maturities of refinancing loans for large export credits, monitoring of geographical and sector limits and relating to firm offers over one year.

Lastly, dynamic liquidity forecasts (taking into account new assets and refinancing assumptions) are carried out regularly in normal and stressed conditions, aimed at:

- defining the amounts and maturities of the various sources of financing that could be raised;
- assessing the capacity of Caisse Française de Financement Local and the SFIL Group to withstand a liquidity shock.

Definition of the transformation risk contained in the specific components monitored in connection with liquidity risk

Transformation risk is part of liquidity risk. It corresponds to the differences in maturity between assets and the resources used to refinance them.

Caisse Française de Financement Local manages this risk using the following two indicators:

- Duration gap
- Weighted average life gap

Duration gap

The difference in maturity between assets and liabilities can lead to liquidity risk. As interest rate risk is controlled (see section 9.2.3.3.), Caisse Française de Financement Local ensures that asset and liability maturities match by keeping the difference in duration between assets and debts benefiting from the legal privilege to three years or less.

Given the method used to hedge interest rate risk (see section 9.2.3.3.), assets and debts benefiting from the legal privilege are all recognized at floating rates after swaps. Caisse Française de Financement Local's balance sheet thus appears to have a single loan opposite a single borrowing. Durations are calculated as follows: "sum of the periods, weighted by the cash flows and discounted at the zero coupon curve rate for the period (t), over the sum of cash flows discounted at the interest rate of the zero coupon curve for the period (t)":

$$D = \frac{\sum_{t=1}^T [(t \times Cft) / (1 + st)^t]}{\sum_{t=1}^T [Cft / (1 + st)^t]}$$

The duration gap between the assets and the liabilities is closely monitored since it is sensitive to fluctuations in interest rates used to calculate the net present value and to significant changes in assets and liabilities.

The duration gap observed in practice remains under the three-year limit, as shown in the table below.

Duration in years	12/31/2016	3/31/2017	6/30/2017	9/30/2017	12/31/2017
Cover pool	7.22	7.35	7.02	7.23	7.44
Privileged liabilities	6.10	6.32	6.36	6.45	6.49
Gap in asset-liability duration	1.13	1.03	0.67	0.77	0.95
Duration gap limit	3	3	3	3	3

Weighted average life gap

Changes in the gap in weighted average life can differ from the changes in the gap in duration over the same period, for the evolution in the duration gap is partly attributable to movements in the interest rate curve. The gap in the weighted average life of the cover pool and the liabilities benefiting from the legal privilege is presented below.

Weighted average life in years	12/31/2016	3/31/2017	6/30/2017	9/30/2017	12/31/2017
Cover pool	7.71	7.88	7.63	7.82	7.99
Privileged liabilities	6.47	6.75	6.86	6.93	6.93
Gap in asset-liability weighted average life	1.24	1.13	0.77	0.88	1.06

Regulatory limit

Current regulations impose a limit of one and a half years on the weighted average life gap between the cover pool, considered on the basis of the minimum amount required to satisfy the legal over-collateralization ratio of 105% and the resources benefiting from the privilege. Caisse Française de Financement Local respects this limit.

9.2.3.3. Interest rate risk

Definition

Interest rate structural risk is defined as the risk of loss incurred in the event of a change in interest rates that would lead to a loss in value of balance sheet and off-balance sheet transactions, excluding any trading portfolio transactions. Since Caisse Française de Financement Local does not have a trading portfolio, it is not concerned by this exception.

There are three different types of interest rate risk:

- the fixed interest rate risk that results from the difference in volume and maturity between fixed rate assets and liabilities, or adjustable rate assets and liabilities for which the interest rate has subsequently been fixed. This risk can result in yield curve parallel shifts, steepening, flattening or rotation;
- the basis risk that results from the gap that may exist in the matching of assets and liabilities indexed on variable rates of different types or index tenors;
- the fixing risk that results, for each index, from the gap between the adjustment dates applied to all the variable rate balance sheet and off-balance sheet items linked to the same tenor.

These risks are generally hedged using derivatives.

Hedging strategy

To limit its impact, interest rate risk is hedged in two stages by Caisse Française de Financement Local:

- In the first stage, all the assets and the liabilities benefiting from the privilege which do not naturally have a floating rate are hedged against Euribor until maturity as soon as they are recorded on the balance sheet. In practice, acquisitions of loan portfolios (in which the unit amount is generally small) are usually macro-hedged. Loans granted individually or bond issues can be micro- or macro-hedged. Hedging of assets and liabilities is more often obtained in using new interest rate swaps, but the same effect can also be obtained whenever possible by the cancelation of swaps of opposite direction.
- In the second stage, Euribor lending and borrowing flows (naturally or after hedges) are swapped against Eonia over a sliding period of maximum two years in order to eliminate the basis risk generated by differences in the tenor (Euribor 1, 3, 6 or 12 months) and the fixing risk due to refixing dates of reference indices that differ for the assets and the liabilities. The residual risk is managed using macro-hedges with a management horizon of one week.

These hedges can be entered into either directly on the market by Caisse Française de Financement Local, or through SFIL, which in turn hedges its resulting position in the market.

Non-privileged debt is not concerned by these hedging operations. In fact, debt contracted by Caisse Française de Financement Local with its shareholder to finance over-collateralization is borrowed either directly with a Eonia index and does not need to be swapped, or with a Euribor index and thus finances assets also indexed on Euribor. Short-term debt owed the Banque de France with a fixed rate (if any) is not hedged, but finances fixed rate assets.

These different types of interest rate risk are monitored, analyzed and managed through the production of gaps (fixed rate, basis and fixing), and/or net present value (NPV) sensitivity indicators.

More specifically, the following indicators are produced in a static view:

- the fixed rate gap, which corresponds to the difference between balance sheet and off-balance sheet assets and liabilities for fixed rate transactions or transactions for which the rate has been fixed. This gap is calculated every month until balance sheet extinction;
- index gaps, which correspond to the difference between balance sheet and off-balance sheet assets and liabilities for a given index tenor that has not yet been fixed. This gap is calculated every month until balance sheet extinction;
- basis gaps, which result from the matching of two index gaps. There are therefore as many basis gaps as there are index pairs;
- the fixing gap, which corresponds, for a given tenor index, to the difference between adjustable rate balance sheet and off-balance sheet assets and liabilities, by fixing date.

Limits governing interest rate risk

The sensitivity of residual positions in fixed rates and variable rates fixed for a determined period of time that remain after the two levels of hedging is monitored on a monthly basis. Limits provide a framework for this sensitivity and are designed to reduce the impact on the value of balance sheet items in the event of a shift in the yield curve or a move in sloping/rotation. They are calibrated so as not to lose more than 6% of equity (i.e. EUR 80 million) with a quantile of 99% calculated based on 2007-2017 historical data.

The net present value (NPV) sensitivity indicators are calculated for a rate shock of 100 x +1 basis point (bp), aiming to limit losses in value in the event of:

- a parallel yield curve shift (limit of EUR 25 million for a shock of 100 x 1bp) to limit the fixed rate or directional rate risk;
- sloping/rotation of the interest rate curve:
 - net present value sensitivity calculation and limiting by time bucket, using four buckets of distinct risks on the yield curve in order to limit risk between distant points on the curve (limit per bucket of EUR 10 million for a shock of 100 x 1bp);
 - net present value sensitivity in terms of absolute value calculation and limiting by time bucket, using four buckets of distinct risks on the yield curve in order to limit risk between near points on the curve, within each bucket (limit per bucket of EUR 20 million for a shock of 100 x 1bp).

Limiting directional risk

The measurement of sensitivity at the end of each quarter is presented below.

Directional risk

Total sensitivity

EUR millions	Limit	12/31/2016	3/31/2017	6/30/2017	9/30/2017	12/31/2017
SENSITIVITY	25.0	(0.5)	(0.1)	(1.6)	1.0	1.5

Measurement of the slope/rotation risk

The quarter-end sensitivity measurements are presented below.

Risk of slope between two distant points on the rate curve

Sum of sensitivities

EUR millions	Limit	12/31/2016	3/31/2017	6/30/2017	9/30/2017	12/31/2017
Short term	10.0	(0.9)	0.1	0.4	(1.7)	0.2
Medium term	10.0	0.3	2.0	(4.5)	(2.4)	(4.6)
Long term	10.0	0.1	(2.6)	1.5	3.8	3.1
Very long term	10.0	0.1	0.4	1.1	1.3	2.7

Risk of slope between two close points on the rate curve

Sum of sensitivities in absolute value

EUR millions	Limit	12/31/2016	3/31/2017	6/30/2017	9/30/2017	12/31/2017
Short term	20.0	4.4	3.3	7.8	10.2	11.6
Medium term	20.0	4.3	5.1	12.4	10.9	14.8
Long term	20.0	8.1	4.9	3.5	7.1	3.6
Very long term	20.0	5.9	5.3	5.6	6.5	6.9

The main risks identified and associated with a low interest rate environment are:

- exposure to a rapid normalization of rates;
- an increase in early repayments not offset by early repayment penalties;
- margin reduction.

Caisse Française de Financement Local has little exposure to interest rate changes and therefore to a rapid normalization of rates: it uses interest rate risk management indicators to manage and monitor exposure to the risks of both parallel and non-parallel shifts in the yield curve, including exposure to the risk associated with the sudden normalization of interest rates.

Caisse Française de Financement Local has little exposure to early repayment risk as almost all of its loan agreements contain early repayment penalty clauses.

Lastly, Caisse Française de Financement Local's business model, based on the refinancing of the local public sector and large export credits, is relatively insensitive to the low interest rate environment. In particular, because Caisse Française de Financement Local does not take sight deposits, it is unaffected by the issue of transformation margin reduction in a low interest rate environment.

Outstanding derivatives

The strategies employed to hedge interest rate risk and foreign exchange risk are illustrated by notional outstanding swaps analyzed in the following table, broken down between external counterparties and an internal counterparty (SFIL), as of December 31, 2017.

Breakdown of outstanding swaps	Notional Absolute value
EUR billions	
Euribor against Eonia	
Macro-hedges	46.8
TOTAL SHORT-TERM SWAPS	46.8
Fixed rate swaps against Euribor	
Micro-hedges on obligations foncières	40.0
Micro-hedges on loans and debt securities	22.3
Macro-hedges on loans	14.5
Subtotal	76.9
Currency swaps	
Micro-hedges on obligations foncières	1.8
Micro-hedges on loans	2.8
Micro-hedges on debt securities	0.6
Subtotal	5.2
TOTAL LONG-TERM SWAPS	82.1

9.2.3.4. Foreign exchange risk

Definition

The foreign exchange risk is defined as the risk of a loss, linked to a change in the exchange rate of currencies vis-à-vis a reference currency. The reference currency of Caisse Française de Financement Local is the euro. The foreign exchange risk reflects a change in the value of assets and liabilities denominated in a currency other than the euro by reason of fluctuations of this same currency vis-à-vis the euro.

Hedging Strategy

Caisse Française de Financement Local's foreign exchange risk management policy is to incur no foreign exchange risk: it enters into cross-currency swaps against the euro for its issues and assets denominated in foreign currency, on initial recognition at the latest and until their final maturity, thereby ensuring that these balance sheet items' principal and interest rates are fully hedged. Floating rate exposures generated by this management policy are incorporated into interest rate risk management. Nonetheless, certain loans to refinance large credit exports denominated in USD may cause a very limited risk of foreign exchange during their drawing phase. This residual risk is handled through the calculation of a very low sensitivity limit.

Foreign exchange risk is monitored using the net foreign exchange position in each currency, calculated on all foreign currency balance sheet receivables, commitments and accrued interest not yet due. Caisse Française de Financement Local's ALM unit and Market and Balance Sheet Risks division ensure that it has no net foreign exchange positions.

9.2.4. Operational risk

9.2.4.1. Definition

Operational risk represents the risk of loss resulting (i) from the lack of adaptation or failure on the part of internal processes, staff, systems or (ii) external events. It includes the risks linked to the security of IT systems, as well as legal and fiscal and compliance risks, but it excludes strategic risk. This definition is in line with the formulation of the Basel Committee. Management procedures for operational risks apply to all of the operating divisions of SFIL in charge of the management of Caisse Française de Financement Local.

9.2.4.2. Organization and governance

SFIL has implemented an organization, procedures and a management system for monitoring and controlling its risks. The Operational Risks and Permanent Control division, within the Risks division, defines the management policy to be used for operational risks, as well as the methods employed to identify and limit them. It pilots operational risk management and relies on a network of correspondents designated in each operating division. Their role is to collect operating incidents and losses, to assess risks and measure key risk indicators with the help of the staff of the Operational Risk and Permanent Control division. The involvement of business line managers strengthens the system's effectiveness.

The operational risk profile in the different operating divisions is presented to the Operational Risks and Permanent Control Committee. It is chaired by SFIL's Deputy CEO, and its members are the entire Executive Committee, including the Chairman of the Executive Board of Caisse Française de Financement Local. It meets quarterly. This committee studies the major operational risks so identified and key risk indicators that have exceeded their alert threshold. It decides as to whether they are acceptable or not and what corrective measures should be taken. It also validates management policies and methods with regard to the management of operational risks. It examines operating incidents that have occurred in the quarter and monitors risk prevention and improvement proposals (permanent control, operational risk management, information security, business continuity).

A synthesis of highlights is presented every quarter to the Risks and Internal Control Committee and the Supervisory Board of Caisse Française de Financement Local in the form of the Quarterly Risks Review. A detailed presentation of action plans, areas for improvement and corrective measures proposed or already implemented to limit operational risk was also organized for Risks and Internal Control Committee on January 25, 2018 and the Executive Board meeting of February 13, 2018.

9.2.4.3. SFIL's policy of operational risk

SFIL has opted for the standard method for calculating equity in respect of operational risk, as provided for by the Basel Committee directives.

SFIL's policy for measuring and managing operational risks consists of regularly identifying and assessing its risk exposure and the existing mitigation and control systems to establish whether or not the level of residual risk is acceptable. The policy applied involves three main processes: the collection and reporting of operational incidents, the mapping of operational risks and the monitoring of key operational risk indicators. This system is complemented by an IT security management policy, a Recovery and Business Continuity Plan (RBCP) and, where necessary, insurance policies to cover specific risks.

9.2.4.4. Operational risk measurement and management

Collection of operational incidents

SFIL has defined an operational incident and loss collection process governed by guidelines and procedures. The systematic collection and analysis of operational incidents provides the information needed to assess SFIL's exposure to operational risk. This operational incident and loss collection process allows SFIL not only to comply with regulatory requirements but also to gather key data to improve the quality of its internal control system.

Various collection thresholds have been defined and communicated to SFIL's operating divisions. The threshold of the mandatory declaration for financial impacts is EUR 2,500. The identification and the analysis of the incidents are the responsi-

bility of the operational risks correspondents with the support of the Operational Risks and Permanent Control division. To this end, SFIL uses an operational risk management tool and in particular a module for incident collection. In function of the results of this analysis, corrective or preventive measures are taken in order to reduce SFIL's exposure to operational risk.

Operational risk identification and assessment

Based on the incidents and losses collected, operational risks are mapped and the resulting mapping is regularly updated. This mapping consists of assessing the operational risks that each SFIL division incurs. It makes it possible to regularly identify and assess these risks, identify existing mitigating factors (systems or controls in place) and determine the residual impacts in order to decide whether or not to accept them. In the event of non-acceptance of the risks, corrective or improvement actions must be implemented (strengthening of systems and procedures, strengthening of the permanent control plan, implementation of systems for monitoring and controlling risks).

The Group is also currently mapping its operational risks by process under a three-year plan to formalize SFIL's processes and activities launched in the second half of 2016. It has defined four main types of activity (steering, asset acquisition, assets and liabilities management until their maturity, and resource provision) and 37 major bank processes within these broad categories. These processes are currently being documented. As part of this plan, the Operational Risks and Permanent Control division has introduced a new methodology for identifying and assessing operational risks by process. This is being deployed as and when SFIL's processes are formalized, in collaboration with the process manager and the operational risk correspondents of the divisions involved, and is gradually replacing the mapping currently in force.

Monitoring of key operational risk indicators

The Operational Risks and Permanent Control division also set up, with SFIL's operating divisions, key risk indicators associated with warning levels. These indicators act as signals of growth in the level of operational risk, a decline in process performance, or of dysfunctions of the internal control system itself. They make it possible to survey in a continuous and dynamic manner the development of operational risks, together with operational risk mapping, which periodically gives a snapshot of SFIL's risk profile.

IT security management

The Operational Risks and Permanent Control division set up a system with a policy and guidelines based on ISO standard 27000, which is applicable to all of SFIL's operating divisions. It is designed to protect information data from any attack on confidentiality, integrity or availability. This policy and these guidelines define the principles applicable by category of security as well as the roles and responsibilities of the different security players. It comprises operational rules, procedures and processes determined with the Information System division, especially those involving the management of authorizations to access SFIL's IT applications and systems.

In addition, a three-year IT security plan has been defined in order to improve the existing systems.

The IT security procedures and changes therein are monitored quarterly by the IT Security and Business Continuity Plan Committee and validated by the Operational Risks and Permanent Control Committee.

Business continuity and crisis management

SFIL has developed a Recovery and Business Continuity Plan (RBCP). It comprises a set of measures and procedures designed to ensure, in various operational crisis scenarios including extreme shocks, that the services or other essential operational tasks that SFIL performs continue, if necessary temporarily or in degraded mode. It also provides for the programmed recovery of these activities so as to limit the losses caused by operation in degraded mode. This plan is based on a business impact assessment that formalizes the needs of SFIL's operating divisions to enable them to restart and resume business based on their criticality.

The RBCP is based on the following three features.

- The operational business continuity plan, which is managed by the Operational Risks and Permanent Control division and documented in guidelines and operational procedures. These guidelines and procedures are regularly updated and the business continuity plan is regularly tested. Disaster recovery sites have been selected for the Issy-les-Moulineaux and Lyon offices to enable the resumption and operational continuation of SFIL's activities. Tests on the functioning of these sites were carried out in March, in May and in June 2017.
- The IT disaster recovery plan, which is managed by the Information Systems division and documented in guidelines and operational procedures. This plan is also regularly tested, with the most recent full live test for SFIL carried out in September 2017.
- The crisis management system, which is managed by the Operational Risks and Permanent Control division. A crisis unit has been identified and regularly tested crisis scenarios have been defined. In particular, a transportation unavailability scenario associated with potential terrorist risk is tested three times a year. A crisis unit exercise, based on a specific scenario, was carried out in November 2017.

New developments in security and business continuity are monitored quarterly by the Information Systems Security and Business Continuity Plan Committee and validated by the Operating Risks and Permanent Control Committee.

Operational risks insurance

To reduce the potential financial impact of operational risks, SFIL has subscribed to several insurance policies. Targeted policies cover the liability of members of the Company's management bodies, professional liability and fraud, as well as multi-risks premises, IT equipment. It also has a policy to protect it from cybercrime. These policies cover SFIL and Caisse Française de Financement Local.

Security of means of payment

Caisse Française de Financement Local does not provide its customers with any means of payment and is not exposed to operational risks in this area.

9.2.5. Legal and tax risks

9.2.5.1. Definition

Legal risk is the risk of any litigation with a counterparty resulting from any misunderstanding, lack or insufficiency that may be attributed to the Company in the exercise of its activities.

9.2.5.2. Organization and monitoring

Caisse Française de Financement Local's monitoring of legal risks focuses on the prevention of litigation, the anticipation of legal developments and the respect of governance principles. The legal risk control is in particular under the responsibility of the SFIL's Legal division, which is part of the General Secretariat. In its capacity, the Legal division has a dual role:

- to advise other SFIL divisions so as to allow them to measure the legal risks inherent in their activities;
- to defend the interests of SFIL and Caisse Française de Financement Local.

Furthermore, the Legal division contributes to the work of various committees:

- Within the framework of its Regulatory Watch Committee, it provides information on the principles underlying legal and regulatory provisions that affect the operations of SFIL and Caisse Française de Financement Local;
- Within the New Products Committee, it advises, as necessary, on the cases presented to it;
- It analyses legal risks associated with the cases presented for the Credit Committee;
- It reviews the cases under litigation and the progress of the procedures at the Loan Sensitivity Reduction Committee meeting. It also expresses its opinion when a loan sensitivity reduction operation involves a legal risk.

The Legal division may also participate in formulating the comments made as part of the audit and internal control operations.

The Board of Directors, Executive Management and Executive Committee of SFIL, as well as the Executive Board and Supervisory Board of Caisse Française de Financement Local receive regular updates on the progress of litigation. A management report regarding the lawsuits is presented at each supervisory board.

SFIL's Finance division is responsible for tax declarations and may consult the SFIL's General Secretariat for tax advice. SFIL relies notably on tax advisory firms of excellent repute for managing its tax risk.

Legal risk

As of December 31, 2017, the number of borrowers in litigation for structured loans was 25⁽¹⁾, compared with 39 as of December 31, 2016 and 131 as of December 31, 2015. Since SFIL's creation, 198 borrowers have dropped their claims against the Group.

Since the entry into force on July 30, 2014 of the law on the securing of structured loan contracts taken out by common law legal entities, the Nanterre Court of First Instance, the Nanterre Commercial Court and the Versailles Court of Appeal have handed down 31 court decisions ruling in favor of Dexia Crédit Local, SFIL and Caisse Française de Financement Local. Only one unfavorable decision, concerning a single non-structured loan, has been handed down, being noted this is a first-instance judgment which is not yet final. Caisse Française de Financement Local, SFIL and Dexia Crédit Local have appealed this decision.

As of December 31, 2017, there were no other significant lawsuits or disputes between Caisse Française de Financement Local and its borrowers.

Fiscal risk

For the record, in 2015, French tax authorities investigated the income declared and the tax paid for 2012 and 2013. Following the tax assessment, the tax authorities expressed their disagreement with the tax treatment of the following two points: the taxation in Ireland of the income from the Dublin branch of Dexia Municipal Agency, which was closed in 2013, and the deductibility of provisions for non-performing loans. In order to safeguard its rights to the disputed adjustment, in 2017 the tax authority initiated a verification procedure relating to the consequences of its previous assessment of taxable income for the 2014 to 2016 fiscal years. The two points of disagreement resulting from the 2015 assessment still held following this tax audit. There were no other new developments.

In order to take into account the risk of an unfavorable outcome in these proceedings, Caisse Française de Financement Local recorded a provision for additional income tax in the amount of EUR 38 million in its 2015 IFRS financial statements. However, Caisse Française de Financement Local does not agree with the position of the tax authorities and started an appeal in 2016 within the framework of legal recourse allowed by current tax regulations. Neither the discussions that took place with the tax authorities nor the new tax audit called into question the assumptions used to calculate the amount provisioned in the accounts.

9.2.6. Risks of non-compliance

9.2.6.1. Definition

Article 10-p of the *arrêté* of November 3, 2014 on the internal control of banks defines non-compliance risk as «the risk of judicial, administrative or disciplinary sanction, of significant financial loss or loss of reputation resulting from failure to comply with the prevailing laws and regulations and professional and ethical standards relating to banking and financial activities or with instructions from the executive body issued in particular pursuant to directives from the decision-making body».

(1) After accounting for a suit which the court had previously declared subject to the statute of limitation.

9.2.6.2. Organization and governance

Pursuant to the provisions of the *arrêté* of November 3, 2014, SFIL uses non-compliance risk mapping and a control plan, which are updated whenever necessary and at least annually, to monitor and control both its own non-compliance risk and that of Caisse Française de Financement Local. This mapping reviews the legislative, regulatory, professional and Group-specific provisions applicable to each line of business or function, and the procedures and controls implemented to ensure compliance with these provisions. The mapping provides a visual indication of the company's exposure to non-compliance risks and defines the boundaries of the bank's non-compliance risk profile. To this end, non-compliance risks are:

- identified and classified;
- assessed (frequency of occurrence and level of severity);
- compared and ranked.

Once the risk areas have been identified through the non-compliance risk mapping, the Compliance division ensures that the risk management system can be used to reduce gross risk.

9.2.6.3. Monitoring of non-compliance and reputation risks

Non-compliance risks associated with the activities of SFIL and Caisse Française de Financement Local concern the following areas:

- employee ethics, prevention of conflicts of interest and the compensation policy;
- protection of the integrity and transparency of financial markets;
- customer protection;
- financial security, in particular compliance with international financial sanctions and the fight against money laundering, financing of terrorism and corruption;
- maintenance of the confidentiality of information and protection of personal data.

At the same time, the Compliance division carries out a regulatory watch to monitor legislative and regulatory changes as well as case law developments liable to impact the Group's compliance activities. It accordingly sits on SFIL's Regulatory Watch Committee. In the event that the institution is impacted by one of these developments, the Compliance division liaises with the divisions concerned to enable them to define and implement the new mechanisms required or, where applicable, propose changes or updates to the associated tools.

The identification and monitoring of regulatory compliance issues in certain specific areas (accounting standards, prudential ratios, control of major counterparty risks, recommendations on IT security, etc.) are the responsibility of SFIL's relevant operating divisions, which duly have appropriate expertise and tools at their disposal.

Moreover, as well as completing the compliance control plan (see section 8.1.5.), the Compliance division controls non-compliance risks:

- by ensuring that its procedural framework is updated. In this regard, in 2017 the Compliance division:
 - completed the anti-money laundering and counter-terrorist financing (AML-CFT) system and the financial security policy relating to the refinancing of large export credits, to take into account regulatory changes;
 - updated the market abuse prevention measures;
 - updated the procedures for protecting customers' interests;
 - set up a steering committee on the protection of personal data ahead of regulatory changes planned for May 2018.
- by continuing its compliance system awareness raising and training initiatives for all of the bank's employees. This involved providing mandatory compliance system training to give employees a full and practical understanding of the importance for the bank of compliance and the systematic use of best practices. This training aims to enable employees to carry out their duties with complete integrity. The Compliance division also dispenses employee training under its AML-CFT obligations. Lastly, it raised the awareness of «insider» employees on market abuse prevention measures. The training system is a key platform for disseminating a compliance culture within the SFIL Group.

The SFIL Group has also set up a formal anti-money laundering and financing of terrorism system. This system, which is adapted to SFIL's local public sector financing activities, has been strengthened to meet the requirements of its export credit refinancing activity, notably in terms of monitoring compliance with embargoes.

EU directive 2015/849 of June 5, 2015 on the prevention of the use of the financial system for the purposes of money laundering or financing terrorism was transposed into French law by ordinance 2016-1635 of December 1, 2016. The directive aims *inter alia* to bring EU law into line with the recommendations of the Financial Action Task Force (FATF) adopted in February 2012. In 2017, the company's AML-CFT system was adapted to incorporate the new provisions and obligations arising from the fourth European anti-money laundering directive.

Lastly, the Compliance division ensures the prevention of reputation risk, which is defined as the risk resulting from customers', counterparties', investors' or regulators' negative perception of the SFIL Group that could undermine its ability to initiate or maintain business relationships and/or its continued access to financing sources.

At the request of the Compliance division, the Communication division has introduced an e-reputation risk monitoring system, and submits a specific quarterly report on this subject to the Compliance division.

10. Commitments granted – commitments received

Commitments granted as of December 31, 2017, are mainly comprised of financing offers granted to SFIL for the refinancing of the export credit business in the amount of EUR 3.0 billion and to a lesser extent the portion not yet paid out of loans granted to French local governments in the amount of EUR 0.1 billion.

Commitments received were principally:

- the authorized overdraft in the current account as stipulated in the financing agreement signed with SFIL for EUR 50 million;
- guarantees received on loans to customers for EUR 2.5 billion.

11. Payment deadlines

In application of articles L.441-6-1 and D.441-4 of the Code of Commerce, Caisse Française de Financement Local must publish every year a breakdown of the balance of the monies it owes to suppliers by due date.

Caisse Française de Financement Local has a very limited number of direct suppliers, since its management is contractually entrusted to its parent company, in conformity with article L.513-15 of the Monetary and Financial Code. Caisse Française de Financement Local usually settles its bills as soon as they are recorded, and the balance of monies owed to suppliers is theoretically always zero. As of December 31, 2017, all supplier accounts were settled. The only supplier debt recorded corresponded to invoices not yet received.

(A) Classes of late payments	Arrears on invoices received by the closing date					TOTAL
	0 day (for information)	1 to 30 days	31 to 60 days	61 to 90 days	91 days and more	
Number of invoices concerned	-	-	-	-	-	-
Total amount of invoices concerned excluding VAT (EUR thousands)	-	-	-	-	-	-
Proportion of total amount of invoices received in the year	-	-	-	-	-	-
(B) Invoices excluded from (A) concerning litigious debt or debt not yet accounted for:						
Number of invoices concerned			-			
Total amount of invoices concerned			-			

Reference payment period: legal or contractual, generally 45 days.

12. Research and development

Since the Company exercises no activity in research and development, no data related to this activity is mentioned in the financial statements.

13. Non-tax-deductible charges and expenses

In accordance with article 223 (4) of the French General Tax Code, no non-deductible expense or charge referred to in article 39-4 of the General Tax Code was made by the Company during the year.

General operating expenses considered as non-deductible following a definitive tax assessment (article 223 (5), article 39-5 and 54 (4) of the General Tax Code) are therefore zero.

14. Social, environmental and societal information

In application of article L.225-102-1 of the Code of Commerce modified by article 225 of law 2010-788 of July 12, 2010 (Grenelle 2 law) and decree 2012-557 of April 24, 2012, Caisse Française de Financement Local must communicate information on social, environmental and societal issues in the Management Report. Since Caisse Française de Financement Local has no salaried employees nor actual premises, social, environmental and societal issues do not apply to this entity.

Social, environmental and societal information concerning SFIL, which manages the activities of Caisse Française de Financement Local, is presented in its annual financial report and on its website.

15. Income for the year

15.1 – INCOME ACCORDING TO IFRS

Caisse Française de Financement Local publishes its financial statements according to IFRS, as adopted by the European Union in order to allow for a better understanding and a better comparability of its financial statements by international investors.

The income statement for 2017 is presented in a synthetic form as follows.

IFRS EUR millions	2015	2016	2017	Change 2017/2016
Interest margin	115	150	185	
Net commissions	(26)	(7)	(12)	
Net result of assets at fair value	(32)	(38)	(33)	
Net result of financial assets	(2)	14	16	
Other income and expense	(0)	(0)	-	
NET BANKING INCOME	55	119	156	31%
General operating expenses	(90)	(91)	(98)	
Taxes	(6)	(7)	(7)	
GROSS OPERATING INCOME	(41)	21	51	143%
Cost of risk	(14)	18	22	
INCOME BEFORE TAX	(55)	39	73	87%
Income tax	(21)	(29)	(32)	
NET INCOME	(76)	10	41	310%

As of December 31, 2017, net income was positive at EUR +41 million, compared with EUR +10 million as of December 31, 2016.

15.1.1. Income restated excluding non-recurring items

Income was strongly influenced by the following factors that should be mentioned in the analysis:

- adjustments in fair value concerning hedges. The application of certain accounting standards or methods (see below) is a source of volatility in Net banking income. The impact of these adjustments was significantly negative in 2015, 2016 and 2017 as shown in the table below.

EUR millions	2015	2016	2017
Fair value adjustments on hedging	(36)	(37)	(37)

For the record, since 2013, fair value adjustments have an effect on existing hedging transactions the Company uses to cover its interest rate and foreign exchange risks. These adjustments impacted asymmetrically the hedged item and its hedging derivative, although the Company applies strict financial hedging rules, and this factor was therefore the cause of major changes in Net banking income:

- fair value adjustments introduced by the standard IFRS 13: Credit Valuation Adjustment / Debit Valuation Adjustment (CVA / DVA), Funding Valuation Adjustment (FVA);
- fair value adjustment of collateralized derivatives: to account for French banks' best practices, the Company chose a valuation against Eonia for derivatives for which it receives cash collateral while the other derivatives remain valued against Euribor. This change in the valuation of hedging derivatives, whereas the valuation of hedged items is not modified, creates inefficiency in hedging relations;
- evaluation of the hedged risk of certain assets and liabilities that are swapped against an Euribor index different from that in the reference curve that serves to value instruments on the balance sheet. The value of the derivative and that of the hedged item follow independent trends, thereby creating hedging inefficiency in accounting;
- adjustment of fair value of derivatives that hedge the foreign exchange risk related to export credit refinancing loans denominated in USD, which in 2017, could not be formally documented as hedging derivatives before the foreign currency loans are recorded on the Company's balance sheet.

These adjustments in the accounting value are recorded in the income statement mainly in the item Net result of assets at fair value.

- the contribution to the support funds created by the French State to solve the problem of sensitive structured loans. The commitment was totally covered by provisions once Caisse Française de Financement Local decided to contribute to the public hospitals support fund in 2015; the impact on the Cost of risk is presented below.

EUR millions	2015	2016	2017
Contributions to support fund for sensitive structured loans	(20)	-	-

- the effect of changes in the income tax rate: in 2017, Caisse Française de Financement Local has taken note of the reduction in corporate income tax to 25% as of 2022. To this end, it reduced its deferred tax assets and recorded a non-

recurring expense of EUR -2 million in its accounts. For the record, in 2016, Caisse Française de Financement Local also took into account legislative measures reducing the tax rate to 28% from 2020, and recorded a non-recurring expense of EUR -14 million.

EUR millions	2015	2016	2017
Adjustments of deferred tax assets	-	(14)	(2)

The recurring income statement for 2016 and 2017 is as follows.

EUR millions	2016			2017		
	Accounting income statement	Non-recurring items	Recurring income statement	Accounting income statement	Non-recurring items	Recurring income statement
NET BANKING INCOME	119	(37)	156	156	(37)	193
Operating Expenses	(98)	-	(98)	(105)	-	(105)
GROSS OPERATING INCOME	21	(37)	58	51	(37)	88
Cost of risk	18	-	18	22	-	22
INCOME BEFORE TAX	39	(37)	76	73	(37)	110
Income tax	(29)	(1)	(28)	(32)	11	(43)
NET INCOME	10	(38)	48	41	(26)	67

Excluding non-recurring items indicated above, Net banking income increased from EUR +156 million in 2016 to EUR +193 million in 2017, and Net income increased from EUR +48 in 2016 million to EUR +67 million in 2017.

15.1.2. Analysis of recurring net income

The improvement in Caisse Française de Financement Local's recurring income in 2017 is due in particular to its sensitivity reduction operations⁽¹⁾, which resulted in:

- an increase in Net banking income, resulting in particular from reversals of provisions against interest on non-performing loans for EUR +31 million in 2017 compared with EUR +5 million in 2016;
- reversals of provisions under Cost of risk for EUR +22 million in 2017 compared with EUR +18 million in 2016.

Meanwhile, the improvement in financing conditions also contributed to the increase in the Interest margin from EUR +150 million in 2016 to EUR +185 million in 2017.

Operating expenses consist mainly of the invoicing of the parent company for Caisse Française de Financement Local's operational management. The increase in Operating expenses between 2016 and 2017 was mainly driven by an increase in IT expenditure.

The income tax charge for the fiscal year amounted to EUR - 43 million; in particular it reflects the non-deductibility of the contribution to the Single Resolution Fund.

15.1.3. First-time application of IFRS 9

The new IFRS 9, which relates to financial instruments and replaces IAS 39, is applicable from January 1, 2018. It has three main strands: classification and measurement, impairment, and hedge accounting. Its application to Caisse Française de Financement Local's activity is presented below.

15.1.3.1. Classification and measurement

The new standard now only provides for three categories of financial instruments: those recognized at amortized cost, those recognized at fair value through profit or loss and those recognized at fair value through other comprehensive income. This classification depends both on the business model in which the financial asset is used and the instrument's contractual features. A financial asset is at amortized cost if:

- the sole purpose for holding it is to collect the associated contractual cash flows;
- these contractual cash flows represent solely payments of principal and interest (SPPI⁽²⁾).

Most of the loans and securities listed as assets of Caisse Française de Financement Local meet these simplicity criteria (hold to collect models and SPPI characteristics) and continue to be recognized at amortized cost. However, certain portfolios will have to be recognized at fair value: these are mainly cash investments under a hold to collect and sell model (fair value recognized directly through other comprehensive income) and structured loans whose financial flows are not SPPI (fair value recognized through profit or loss). Furthermore, sensitivity reduction operations and certain restructurings of non-SPPI loans as SPPI loans are now systematically considered as capable of derecognition, leading to immediate recognition of the early repayment penalty:

(1) Within the framework of the successful policy to reduce the interest rate sensitivity in 2016 and the confirmation of legal decisions favorable to the bank, Caisse Française de Financement Local was able to hone, in a reasonable and prudent manner, the methods it uses to estimate the recoverability of flows of non-performing loans on its balance sheet. In particular, in order to account for the impact of the spread of payments, the implementation of this approach, which is in compliance with IFRS, makes it no longer systematically necessary to estimate the total amount of interest to account for hypotheses of future recovery. Thus, the net interest rate expense is improved through a recovery of provisions in the amount of EUR 31 million, recorded as of December 31, 2017.

(2) SPPI: Solely Payments of Principal and Interest

- in equity for the first time application of IFRS 9 for restructurings that occurred prior to January 1, 2018;
- in the income statement for restructurings that will occur from January 1, 2018.

15.1.3.2. Impairment

In accordance with the new IFRS 9, loans and securities measured at amortized cost or at fair value through other comprehensive income will be classified in one of three levels:

- level 1: performing loans;
- level 2: loans whose risk has deteriorated significantly;
- level 3: non-performing loans.

Provisions will be recorded in respect of all these assets, including performing loans. The related impairment will be based on forward-looking scenarios (defined by probability of occurrence), and will take into account expected losses over the next 12 months (level 1) or the asset's life (levels 2 and 3).

In addition, changes in the credit risk of loans and securities recognized at fair value through profit or loss will be included in their valuation.

15.1.3.3. Hedge accounting

Pending the entry into force of the future macro-hedging standard, Caisse Française de Financement Local has chosen to continue applying IAS 39 in this area.

15.1.3.4. Expected impacts on future equity and results

The first-time application of IFRS 9 to transactions on Caisse Française de Financement Local's balance sheet as of January 1, 2018 will have a limited impact on equity as regards the new provisioning methods, but a more significant impact from the classification and measurement standpoint.

Overall, the first-time application of the standard will have a positive impact of less than 1% on the CET1 solvency ratio.

IFRS 9 will also have an impact on future results due mainly to changes in the fair value of non-SPPI loans, which will lead to increased income volatility. This standard will therefore increase the volatility of NBI in a way unrelated to Caisse Française de Financement Local's activity, as its business model involves holding all loans until maturity. It will therefore be necessary to be able to isolate these impacts and remove them from the Company's performance analyses.

15.2. INCOME ACCORDING TO FRENCH GAAP

Net income for the year 2017 is presented below in a synthetic manner.

French GAAP EUR millions	2015	2016	2017	Change 2017/2016
Interest margin	186	179	127	
Net commissions	(26)	(7)	(12)	
Provisions and income on trading portfolio	0	(0)	0	
Provisions and income on securities	21	(9)	3	
Other income and expense	(0)	-	-	
NET BANKING INCOME	181	163	118	(28)%
General operating expenses	(90)	(91)	(98)	
Taxes	(6)	(7)	(7)	
GROSS OPERATING INCOME	85	65	13	(80)%
Cost of risk	(14)	18	22	
OPERATING INCOME	71	83	35	(58)%
Income (loss) on fixed assets	(5)	-	-	
Income tax	(96)	(16)	(5)	
NET INCOME	(30)	67	30	(56)%

The Company's business is piloted according to IFRS (as adopted by the European Union). The French GAAP financial statements are published in accordance with legal requirements and serve as a base to calculate income subject to corporate income tax.

Readers are reminded that the accounting treatment for recognition of the penalties due to the early repayment of loans and swap unwinding payments for termination of hedging swaps in the French GAAP accounts differs from the treatment applied in the accounts prepared pursuant to IFRS. Pursuant to IFRS, cash payments and penalties are usually amortized, while they are usually recognized immediately in Net banking income, according to French GAAP. This accounting treatment may lead to recognition of the results earlier than would a systematic amortization approach. These penalties and cash payments are generated by early reimbursements, but also by renegotiations, which generally accompany active debt management by borrowers, as well as swaps which are cancelled in order to back assets to liabilities directly. The methods employed, which have not changed in the last three years, are described in the rules of presentation and evaluation of the financial statements in the notes to the financial statements in the sections entitled Customer loans, Micro-hedge transactions and Macro-hedge transactions.

Net banking income dropped by 28%, i.e. EUR -45 million, as compared with the same period in 2016, from EUR +163 million to EUR +118 million.

This decrease was due in particular to Interest margin, which decreased by EUR -52 million from EUR +179 million to EUR +127 million. The Interest margin corresponds to the difference between assets income and the cost of liabilities (fully hedged against interest rate and foreign exchange risks). It varies depending on whether it is presented under IFRS (economic view) or French GAAP (see above), which can make changes difficult to interpret, especially in years of very active local government entity debt management (including sensitivity reduction operations). This was particularly the case in 2016, which explains the high level of interest margin for that year.

At the same time, Net commissions increased compared with 2016, representing a net charge of EUR -12 million.

Lastly, Provisions and income on securities increased by EUR +12 million, reflecting a provision reversal in 2017 related to the increase in market value of placement securities.

Operating expenses consisted mainly of the invoicing of the parent company for Caisse Française de Financement Local's operational management. The increase in operating expenses between 2016 and 2017 was mainly driven by an increase in IT expenditure.

The Cost of risk was positive at EUR +22 million in 2017, up EUR +4 million compared with 2016. This improvement results from the positive effects generated by the structured loan sensitivity reduction policy.

There was a EUR -5 million income tax charge for the fiscal year.

Net income fell from EUR +67 million in 2016 to EUR +30 million in 2017.

15.3. YIELD OF THE ASSETS

Article R.511-16-1 of the Monetary and Financial Code, introduced by the decree 2014-1315 of November 3, 2014, requires that in their annual financial report, credit institutions publish the yield of their assets, defined as the ratio between the net result and the total of the balance sheet. In 2017, this ratio equals +0.06% in IFRS and +0.05% in French GAAP.

16. Proposed allocation of net income

In previous years, Caisse Française de Financement Local has made the following distributions:

Year of distribution	Distributed from the year's income	Amount distributed EUR	Amount per share EUR	Number of shares
2000	1999	3,600,000	1.20	3,000,000
2001	2000	-	-	4,000,000
2002	2001	-	-	4,500,000
2003	2002	-	-	4,500,000
2004	2003	120,000,000	24.00	5,000,000
2005	2004	62,000,000	10.00	6,200,000
2006	2005	84,320,000	12.40	6,800,000
2007	2006	116,280,000	15.30	7,600,000
2008	2007	70,080,000	8.00	8,760,000
2009	2008	113,520,000	12.00	9,460,000
2010	2009	133,560,000	12.60	10,600,000
2011	2010	110,075,000	9.25	11,900,000
2012	2011	15,080,000	1.16	13,000,000
2013	2012	-	-	13,150,000
2014	2013	-	-	13,150,000
2015	2014	-	-	13,150,000
2016	2015	-	-	13,150,000
2017	2016	35,110,500	2.67	13,150,000

The Ordinary Shareholders' Meeting will be asked to distribute a dividend in the amount of EUR 50 millions and to vote a resolution to allocate net income as follows (in euros).

ALLOCATION OF NET INCOME	EUROS
Net income for the year	29,705,091.31
Legal reserve (5%)	(1,485,257.57)
Income available	28,219,836.74
Retained earnings	23,640,014.37
Income available for distribution	51,859,851.11
Proposed dividends	(49,950,000)
Retained earnings after allocation	1,909,851.11

17. Outlook for 2018

In 2018, Caisse Française de Financement Local and its parent company SFIL will aim to:

- maintain their role as a major player in the market for loans to French local governments and public hospitals, within the framework of the system established with La Banque Postale;
- continue their key role as refinancer of partner banks of French exporters, for large export credits.

The bulk of the sensitivity reduction work has been completed and by end-2018 the most at-risk outstandings, i.e. those indexed on EUR/CHF, will be reduced to a marginal level. This activity, which generally involves granting new loans to the local government entities concerned, will now be scaled down. In addition, the already very significant reduction in the number of lawsuits issued in the year ended December 31, 2017, is expected to continue in 2018.

In addition, as announced on March 8, 2018, SFIL's refinancing export credit system may be expanded to loans designed to finance projects considered strategic for France without necessarily having to be linked to an underlying export. These projects will benefit from a new guarantee of the French State, and may be refinanced by Caisse Française de Financement Local through an enhanced guarantee arrangement.

In 2018, new loans will be included in Caisse Française de Financement Local's cover pool representing exposures to the French local public sector and the French State.

To cover its financing requirements, in 2018 Caisse Française de Financement Local plans to issue between EUR 4 billion and EUR 6 billion of *obligations foncières* with a long average maturity, adapted to the profile of the assets financed. Its program will mainly be carried out through a number of benchmark issues in euros and private placements adapted to the needs of its broad investor base.

Lastly, from a macro-economic point of view, as in 2017, two significant background issues will be closely monitored in 2018:

- developments in the regulatory environment;
- market volatility in a context influenced by the perspectives for a quantitative easing exit strategy announced by the European Central Bank, the provisions linked to Brexit and the geopolitical environment.

Breakdown of cover pool as of December 31, 2017

EUR millions	12/31/2017				12/31/2016	
	Direct exposure		Indirect exposure		Total	
	Loans	Bonds	Loans	Bonds		
COUNTRY						
France						
State:						
- export refinancing	-	-	218	-	218	-
- other	5	-	113	-	118	98
Banque de France	1,707	-	-	-	1,707	3,685
Regions	1,813	325	261	-	2,399	2,051
Departments	6,834	-	184	-	7,018	6,986
Municipalities	15,706	19	440	-	16,165	16,648
Groups of municipalities	10,935	83	154	-	11,172	11,004
Public sector entities:						
- health	6,219	-	-	-	6,219	6,310
- social housing	1,291	-	-	-	1,291	1,421
- other	875	243	1	-	1,119	945
Credit institutions	370	324	-	-	694	650
Subtotal	45,755	994	1,371	-	48,120	49,798
Germany						
<i>Länder</i>	-	275	-	-	275	515
Subtotal	-	275	-	-	275	515
Austria						
<i>Länder</i>	-	-	187	-	187	191
Subtotal	-	-	187	-	187	191
Belgium						
Regions	8	-	22	-	30	44
Communities	-	-	-	-	-	50
Public sector entities	54	-	-	-	54	60
Credit institutions	-	57	-	-	57	-
Subtotal	62	57	22	-	141	154
Canada						
Provinces	-	-	-	-	-	22
Communities	161	-	-	-	161	172
Public sector entities	35	-	-	-	35	129
Subtotal	196	-	-	-	196	323
Spain						
State	-	200	-	-	200	200
Regions	-	65	-	-	65	104
Municipalities	80	-	-	-	80	88
Subtotal	80	265	-	-	345	392
United States						
Federated States	-	253	-	-	253	252
Subtotal	-	253	-	-	253	252

EUR millions	12/31/2017					12/31/2016
	Direct exposure		Indirect exposure		Total	Total
	Loans	Bonds	Loans	Bonds		
COUNTRY						
Italy						
State	-	543	-	-	543	541
Regions	-	1,975	-	-	1,975	2,043
Provinces	-	522	-	-	522	566
Municipalities	8	1,843	-	-	1,851	1,973
Subtotal	8	4,883	-	-	4,891	5,123
Japan						
Municipalities	-	25	-	-	25	25
Subtotal	-	25	-	-	25	25
Norway						
Credit institutions	-	70	-	-	70	-
Subtotal	-	70	-	-	70	-
Portugal						
Municipalities	17	-	-	-	17	20
Public sector entities	5	-	-	-	5	6
Subtotal	22	-	-	-	22	26
United Kingdom						
State	-	-	-	232	232	320
Subtotal	-	-	-	232	232	320
Sweden						
Municipalities	18	-	-	-	18	18
Credit institutions	-	100	-	-	100	-
Subtotal	18	100	-	-	118	18
Switzerland						
Cantons	263	-	40	-	303	386
Municipalities	493	-	-	-	493	556
Public sector entities	90	-	-	-	90	91
Subtotal	846	-	40	-	886	1,033
Supranational						
International organizations	28	-	-	-	28	32
Subtotal	28	-	-	-	28	32
TOTAL COVER POOL	47,015	6,922	1,620	232	55,789	58,202

Loans and securities are off premium / discount. Loans and securities denominated in foreign currencies are recorded at their euro swapped value. Loans and bonds are presented after specific impairments. In addition to these impairments, Caisse Française de Financement Local makes collective and sectorial impairments.

Income for the last five years

	2013	2014	2015	2016	2017
FINANCIAL POSITION					
Share capital (EUR millions)	1,315	1,315	1,315	1,315	1,350
Number of shares	13,150,000	13,150,000	13,150,000	13,150,000	13,500,000
RESULTS OF OPERATIONS (EUR MILLIONS)					
Revenues ⁽¹⁾	2,287	1,177	2,172	2,476	575
Income before income tax, amortization, depreciation and contingencies net of reversals	94	63	71	86	14
Income tax	(5)	(9)	(96)	(16)	(5)
Income after income tax, amortization, depreciation and contingencies net of reversals	(21)	8	(30)	67	30
Exceptional distribution	-	-	-	-	-
Dividend ⁽²⁾	-	-	-	35	50
PER SHARE DATA (EUR)					
Revenues	173.89	89.54	165.16	188.28	43.72
Income after income tax, before amortization, depreciation and contingencies net of reversals	6.74	4.12	(1.92)	5.37	0.64
Income tax	(0.42)	(0.69)	(7.34)	(1.19)	(0.40)
Income after income tax, amortization, depreciation and contingencies net of reversals	(1.56)	0.59	(2.30)	5.08	2.26
Exceptional distribution	-	-	-	-	-
Dividend per share ⁽²⁾	-	-	-	2.67	3.70

(1) Revenues are comprised of the macro-hedging items:
 - interest and related income, netted of macro-hedging expense;
 - commission income;
 - net income on foreign exchange transactions;
 - other operating income.

(2) For 2017: proposed distribution for the fiscal year.

Report of one of the statutory auditors, appointed as independent third-party, on the social, environmental and societal information published in the management report

Year ended December 31, 2017

This is a free English translation of the statutory auditors' report issued in French and is provided solely for the convenience of English-speaking readers. This report should be read in conjunction with, and construed in accordance with, French law and professional standards applicable in France.

To the Shareholders' Meeting,

In our capacity as statutory auditor of Caisse Française de Financement Local, and appointed as independent third-party, for whom the certification request has been approved by the French National Accreditation Body (COFRAC) under the number 3-1048⁽¹⁾, we hereby present you with our report on the social, environmental and societal information prepared for the year ended December 31, 2017 (hereinafter the "CSR Information"), presented in the management report pursuant to Article L.225-102-1 of the French Code of Commerce (Code de commerce).

RESPONSIBILITY OF THE COMPANY

The Executive Board is responsible for preparing a management report including CSR Information in accordance with the provisions of Article R.225-105-1 of the Code of Commerce.

INDEPENDENCE AND QUALITY CONTROL

Our independence is defined by regulatory texts, the profession's Code of Ethics as well as by the provisions set forth in Article L.822-11 of the Code of Commerce. Furthermore, we have set up a quality control system that includes the documented policies and procedures designed to ensure compliance with rules of ethics, professional auditing standards and the applicable legal texts and regulations.

RESPONSIBILITY OF THE STATUTORY AUDITOR

Based on our work, our responsibility is:

- to attest that the CSR Information required under article R.225-105-1 of the Code of Commerce is presented in the management report or, in the event of omission, is explained pursuant to the third paragraph of article R.225-105 of the Code of Commerce;
- to express a reasoned opinion on the accuracy of information included in the management report and, if need be, the explanations relating to the omission of some of the CSR Information required under the third paragraph of article R.225-105 of the Code of Commerce;
- the procedures performed to conduct our mission.

Our work was carried out by a team of two people in March 2018. To assist us in conducting our work, we referred to our corporate responsibility experts.

We conducted the following procedures in accordance with professional guidance issued by the French national institute of statutory auditors (Compagnie nationale des commissaires aux comptes) and with the *arrêté* of May 13, 2013 determining the methodology according to which the independent third party entity conducts its assignment.

As indicated in the management report, the company does not disclose any CSR information because of the absence of employees and physical footprints. Our work consisted in the appreciation of the pertinence of the explications related to total absence of CSR information.

CONCLUSION

Based on these procedures:

- we attest the relevance of the explanations relating to the total omission of CSR Information in the management report;
- we do not have any observation to mention about the provided explanations.

Neuilly-sur-Seine, March 29, 2018.

French original signed by one of the statutory auditors:

DELOITTE & ASSOCIÉS
Sylvie Bourguignon

⁽¹⁾ the scope of which is available at www.cofrac.fr

Report on corporate governance

prepared in accordance with article L.225-68 of the Code of Commerce

This report presents Caisse Française de Financement Local's governance, detailing notably the role and composition of its Supervisory Board and Executive Board, and the compensation of members of management and supervisory bodies.

To prepare this report, Caisse Française de Financement Local refers to:

- the Code of Commerce, as a commercial company;
- the Monetary and Financial Code, as a credit institution;
- relevant European regulations for credit institutions;
- the provisions of the ordinance of August 20, 2014, on the governance and operations on the equity of companies with public sector shareholders.
- the governance provisions adopted by its parent company SFIL, which opted to refer to the AFEF/MEDEF code of corporate governance as a reference for the SFIL Group.

This report was drawn up by Caisse Française de Financement Local's Supervisory Board which gathered the appropriate information from the Company's Executive Board and its parent company's General Secretariat.

Caisse Française de Financement Local has two main missions, as follows:

- to refinance public sector loans within the framework of funding French local governments and public hospitals;
- to grant loans to SFIL in order to fund large export credits within the framework set up by the French State. Such refinancing benefits from an irrevocable and unconditional 100% guarantee by the French State.

These two activities are based on the issue of *obligations foncières* and use of other financial resources benefiting from the same privilege. The objective is to provide optimal financing conditions for large export credits as well as French local governments and public hospitals through a high rating and impeccable risk management.

For the record, Caisse Française de Financement Local is a legally independent company with its own Supervisory Board and Executive Board. However, in order to preserve the privilege enjoyed by holders of *obligations foncières* and other privileged debt securities, the law stipulates that a *société de crédit foncier* is not allowed to employ staff directly and must entrust the management of all its operations to a credit institution with which it signs an agreement (article L.513-15 of the Monetary and Financial Code). This is because employees would have a priority that would supersede any other claim in the event of bankruptcy or liquidation, whereas the management agreement, which benefits from the privilege granted by the law on *sociétés de crédit foncier*, is *pari passu* with the holders of *obligations foncières* and other privileged debt securities. Caisse Française de Financement Local has entrusted the management of its operations to SFIL, since 2013. There are divisions or departments at SFIL that handle transactions conducted in the name of Caisse Française de Financement Local.

1. Caisse Française de Financement Local's Governance

Caisse Française de Financement Local is a *société anonyme à directoire et conseil de surveillance*, a joint-stock corporation with an Executive Board and a Supervisory Board, governed by the provisions of articles L.210-1 *et seq* of the Code of Commerce. Its activity is governed by articles L.511-1 *et seq* (credit institutions) and L.513-2 *et seq* (*sociétés de crédit foncier*) of the Monetary and Financial Code.

In terms of governance, Caisse Française de Financement Local implements, for the areas relating to it, the provisions of its parent company that refer to the AFEF/MEDEF code. However, certain differences exist. Thus, the absence of independent members on its Supervisory Board reflects a choice related to the status and role conferred on Caisse Française de Financement Local under arrangements for the SFIL Group's refinancing of the French public sector and exports, as well as to the Company's shareholder structure. In addition, Caisse Française de Financement Local is wholly owned by SFIL, a public development bank that complies with the rules relating to the independence of members of its Board of Directors. Also, as a result of this organization and the company's shareholder structure, it does not implement the recommendations relating to the number of shares held by members of the Board of Directors and to the convening at least once a year of a Supervisory Board' meeting without the presence of members of the Executive Board. With regard to the existence of a succession plan for members of supervisory and management bodies, a procedure will be proposed in 2018.

It should be noted that in 2017, decisions made at the Shareholders' Meetings led to a better gender balance on the Supervisory Board.

Meanwhile, as the Monetary and Financial Code authorizes an entity to refer to its parent company's Governance and Appointments Committee and Compensation Committee for the definition of its appointments and compensation policy, Caisse Française de Financement Local's Supervisory Board has decided not to create a specific committee at its level but to rely on those of SFIL. Similarly, both SFIL's Financial Statements Committee and its Risks and Internal Control Committee handle issues concerning Caisse Française de Financement Local. The documents presenting these issues are included in the files presented to the Supervisory Board, which is also briefed on these committees' discussions when they are related to the Company.

1.1 – THE SUPERVISORY BOARD

1.1.1. The role of the Supervisory Board

The Supervisory Board exercises permanent control over the Executive Board's management of the Company. The Shareholders' Meeting appoints the Supervisory Board's members for four-year terms, on the basis of their qualifications and potential contribution to the Company. Prior to their appointment, SFIL's Governance and Appointments Committee reviews their respective skills and qualifications using the Fit and Proper test process. The Ordinary Shareholders' Meeting of May 30, 2017 reappointed Philippe Mills, François Laugier, Florent Lecinq and Sami Gotrane as members of the Supervisory Board and decided not to reappoint Stéphane Costa de Beauregard. It appointed two new Supervisory Board members, Nathalie Argourd and Anne Crépin. The effect of these decisions was to strengthen the Board's debt management and export credit refinancing skills, while increasing the number of Supervisory Board members from six to seven. They also made it possible to achieve a more balanced representation of men and women in this body, in accordance with the related legal provisions.

The Supervisory Board meets at least once a quarter, with both the statutory auditors and the Company's Specific Controller in attendance. During the 2017 fiscal year, the Board met four times, with an attendance rate of 89%.

The Chairman of the Supervisory Board or of the Executive Board informs the Board's members of meeting agendas, allowing enough time before the meetings take place for them to review the items for discussion, and provides a file containing the memos or documents relating to said items. The files containing the information and documents sent to the Board enable it to form a clear, reliable and comprehensive view of the Company's situation, profitability and development. At the Supervisory Board meetings, the Executive Board reviews and comments on the agenda items, using summary presentations where appropriate. The Supervisory Board issues opinions on strategic choices, makes recommendations and, where appropriate, commissions ad hoc studies, which are reviewed at subsequent meetings. The agenda follows a standard format: minutes of the previous meeting, activity report for the past and current quarters, including the monitoring of issuance conditions, presentation of the financial statements, asset acquisitions from La Banque Postale and refinancing of large export credits. Specific topics are included on the agenda depending on the time of year, such as the report on internal control and the report on risk measurement and monitoring, pursuant to articles 258 *et seq* of the *arrêté* of November 3, 2014, and the information to be published on asset quality and the level and sensitivity of interest rate risk, pursuant to article 13 of CRBF regulation 99-10. The Supervisory Board pays particular attention to Caisse Française de Financement Local's acquisition of public sector assets from La Banque Postale and to the loans it makes to refinance large export credits. It closely monitors execution of Caisse Française de Financement Local's issuance program and the performance of its *obligations foncières* on the primary and secondary markets. The Supervisory Board believes that the optimization of Caisse Française de Financement Local's financial conditions – irrespective of market conditions and the ratings assigned by Standard and Poor's, Moody's and Fitch – depends on the extent to which investors recognize the excellent quality of the company's assets and its minimal level of customer counterparty, market counterparty, interest rate and liquidity risk. The Supervisory Board pays particular attention to the reports that the Executive Board submits to it on these issues and to the transparency of the related disclosures to investors. The Supervisory Board is also briefed on requests from the Company's regulators and the information that its management provides in response.

In 2017, in addition to the questions related to the management of the Company that are under its responsibility, the Supervisory Board paid particular attention in its governance to its issuance strategy, issue ratings, purchasing of public sector loans from La Banque Postale, refinancing of large export credits, monitoring of litigation, ongoing application of its strategy to reduce the sensitivity of structured loans, assistance rendered by its servicer and parent company, and risks especially with the review for approval of the ICAAP and ILAAP reports, recovery plan and Recovery and Business Continuity Plan. In 2017, the Supervisory Board also reviewed in detail the preparatory work for the implementation of IFRS 9, which came into force on January 1, 2018, with a number of presentations made on this subject throughout the course of the year.

The Supervisory Board called an Ordinary and Extraordinary Shareholders' Meeting on May 30, 2017. The Ordinary Shareholders' Meeting was called notably to:

- approve the financial statements and the appropriation of income;
- approve the Company's regulated agreements and commitments;
- review the composition of the Supervisory Board (see above);
- renew for six years the term of office as principal Statutory Auditor of Deloitte & Associés and appoint Ernst & Young et Autres as a new principal Statutory Auditor for six years, to replace Mazars.

The Extraordinary Shareholders' Meeting was called to:

- approve a EUR 35 million cash capital increase by the creation of new shares, and amend the by-laws accordingly;
- approve the amendment of the provisions of the by-laws relating to the statutory auditors in order to comply with (i) the provisions of instruction no. 2016-I-07 and (ii) the provisions of article L.823-1 of the Code of Commerce amended by law no. 2016-1691 of December 9, 2016 (so-called Sapin II law).

1.1.2. Composition of Supervisory Board

Supervisory Board (as of December 31, 2017)

Philippe Mills
Chairman

François Laugier
Vice Chairman

Nathalie Argourd
Member of the Supervisory Board

Anne Crépin
Member of the Supervisory Board

Béatrice Gosserez
Member of the Supervisory Board

Sami Gotrane
Member of the Supervisory Board

Florent Lecinq
Member of the Supervisory Board

1.2 - THE EXECUTIVE BOARD

1.2.1. The role of the Executive Board

The Executive Board is in charge of Caisse Française de Financement Local's management and administration, with the capacity to represent and commit it. As such, its role is to take all decisions impacting Caisse Française de Financement Local's activity and results. Moreover, the Executive Board is the first guarantor of the proper functioning of Caisse Française de Financement Local's internal control procedures (see section 8.1 of the Management Report).

More specifically, the Executive Board's responsibilities include:

- convening Shareholders' Meetings;
- deciding, by delegation from the Extraordinary Shareholders' Meeting, to increase the share capital and/or determining the terms of this increase, and if necessary carrying out a capital reduction;
- amending the share capital at any time following the conversion of convertible bonds, subscriptions using rights detached from hybrid securities containing share subscription options, and the exercise of share subscription options.
- issuing *obligations foncières* and registered covered bonds;
- acquiring assets under the two assignments entrusted by the French State to Caisse Française de Financement Local: refinancing of loans to French local governments and public hospitals and refinancing of large export credits;
- selling assets;
- managing balance sheet and off-balance sheet transactions;
- validating the Company's risk appetite and its application in the risk analysis and measurement oversight systems and procedures;
- defining SFIL's servicing conditions, notably by (i) approving and monitoring the management contract and amendments thereto, the service level agreement and the associated quality indicators, and (ii) approving Caisse Française de Financement Local's operational management policies;
- preparing the quarterly financial and activity reports for submission to the Supervisory Board;
- preparing the financial statements in accordance with IFRS and French GAAP.

Furthermore, for activities delegated to SFIL, Caisse Française de Financement Local's Executive Board is specifically informed of and, if appropriate, required to act on, the following:

- litigation;
- risks, including non-compliance risks;
- internal control.

In 2017, the Executive Board was composed of five members. Its members are appointed by Caisse Française de Financement Local's Supervisory Board after approval by SFIL's Governance and Appointments Committee. The term of office of the members of the Company's Executive Board is set at four years.

The Executive Board meets on average twice a month; each quarter a meeting is devoted to preparing the next Supervisory Board meeting. One-off meetings may also be held on the basis of current events and urgent subjects in need of approval.

The statutory auditors are invited to Executive Board meetings if their attendance is mandatory, which applies specifically for the review of the annual or interim financial statements. Depending on the agenda items, the Chairman of the Executive

Board may decide, in particular on the proposal of another Board member, to invite any person that he or she deems useful to present a subject or assist with preparatory discussions of said items.

1.2.2. Composition of the Executive Board

Executive Board (as of December 31, 2017)

Gilles Gallerne
Chairman

Romain Bailly
Chief Executive Officer
Member of the Executive Board

Patrick Galland
Member of the Executive Board

Olivier Eudes
Member of the Executive Board

Emmanuel Moritz
Member of the Executive Board

2. Directorships and positions of members of supervisory and management bodies

In application of article L.225-102-1 of the Code of Commerce, the following list presents the directorships and positions exercised in 2017 by every member of the supervisory and management bodies of Caisse Française de Financement Local who served during the year.

2.1 - THE SUPERVISORY BOARD

CHAIRMAN

Philippe Mills

52 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: May 30, 2017 - 2021

Date of first mandate: January 31, 2013

Principal function: Member of the Board of Directors, Chief Executive Officer, SFIL

Other mandates and responsibilities:

- Chairman of the Executive Committee, SFIL
- Alternate Expert, Board of Directors, European Investment Bank (EIB)
- Chairman of the Board of Directors, European Association of Public Banks (EAPB).

VICE CHAIRMAN

François Laugier

53 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: May 30, 2017 - 2021

Date of first mandate: January 31, 2013

Principal function: Deputy Chief Executive Officer, SFIL

Other mandates and responsibilities: Member of the Executive Committee, SFIL

MEMBERS

Nathalie Argourd (since May 30, 2017)

46 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: May 30, 2017 - 2021

Date of first mandate: May 30, 2017

Principal function: Director, Middle Office and Customer's Debt Management Applications, SFIL

Other mandates and responsibilities: none

Anne Crépin (since May 30, 2017)

48 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: May 30, 2017 - 2021

Date of first mandate: May 30, 2017

Principal function: Deputy Director, Export Credit, SFIL

Other mandates and responsibilities: none

Stéphane Costa de Beauregard (until May 30, 2017)

51 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: January 31, 2013 – May 30, 2017

Date of first mandate: January 31, 2013

Principal function: Director, Customer's Debt Management, SFIL

Other mandates and responsibilities: Member of the Executive Committee, SFIL

Béatrice Gosserez

52 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: May 25, 2016-2020.

Date of first mandate: December 12, 2012

Principal function: General Secretary, SFIL

Other mandates and responsibilities: Member of the Executive Committee, SFIL

Sami Gotrane

53 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: May 30, 2017 - 2021

Date of first mandate: January 31, 2013

Principal function: Director, Treasury and Financial Markets, SFIL

Other mandates and responsibilities:

- Member of the Executive Committee, SFIL
- Chairman, CTG Financial Consulting

Florent Lecinq

42 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: May 30, 2017 - 2021

Date of first mandate: February 25, 2013

Principal function: Chief Financial Officer, SFIL

Other mandates and responsibilities: Member of the Executive Committee, SFIL

2.2 - THE EXECUTIVE BOARD**CHAIRMAN****Gilles Gallerne**

54 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: January 31, 2017 – 2021

Date of first mandate: January 1, 2008

Principal function: Director, CAFFIL Coordination, SFIL

Other mandates and responsibilities:

- Member of the Executive Committee, SFIL
- Member of the Board, Association Française des Sociétés Financières (ASF)

CHIEF EXECUTIVE OFFICER**Romain Bailly**

36 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: January 31, 2017-2021

Date of first mandate: December 7, 2016

Principal function: Head of CAFFIL Coordination division, SFIL

Other mandates and responsibilities: none

MEMBERS**Olivier Eudes**

49 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: January 31, 2017 - 2021

Date of first mandate: May 27, 2015

Principal function: Director, Financial Markets, SFIL

Other mandates and responsibilities: Manager, SCI Phoenix

Patrick Galland

51 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: January 31, 2017 - 2021

Date of first mandate: December 7, 2016

Principal function: Director, Coordination Financial Performance Management division, SFIL

Other mandates and responsibilities:

- Member of the Board of Directors, SFIL
- Member of the Risk and Internal Control Committee, SFIL

Emmanuel Moritz

42 years old – French nationality

Professional address: SFIL - 1-3, rue du Passeur de Boulogne 92130 Issy-les-Moulineaux

Date mandate begins and ends: January 31, 2017 - 2021

Date of first mandate: January 31, 2013

Principal function: Director, Credit Risks, SFIL

Other mandates and responsibilities: none

3. Compensation of members of supervisory and management bodies

In 2017, Caisse Française de Financement Local paid no compensation to the members of its supervisory and management bodies who were employees of SFIL and who exercised their mandates with no specific compensation, except for the Chairman of the Supervisory Board, who is also a member of the parent company's Board of Directors and only in this role receives any compensation.

Readers are reminded that Caisse Française de Financement Local has no compensation committee and that reference is made to the Appointments and Compensation Committees that exist at the level of its parent company, SFIL.

4. Statutory auditors

The statutory auditors of Caisse Française de Financement Local are:

Mazars (until May 30, 2017)

Exaltis – 61, rue Henri Regnault – 92075 – La Défense Cedex

Represented by Anne Veaute, Partner

Not re-appointed by the Shareholders' Meeting of May 30, 2017.

Deloitte & Associés

185, avenue Charles de Gaulle – 92524 Neuilly-sur-Seine Cedex

Represented by Sylvie Bourguignon, Partner

Re-appointed by the Shareholders' Meeting of May 30, 2017, for a term of six years, i.e. until after the Shareholders' Meeting called to approve the financial statements for the year ending December 31, 2022.

Ernst & Young et Autres

1-2, place des Saisons – 92400 Courbevoie – Paris-La Défense 1

Represented by Vincent Roty, Partner

Appointed by the Shareholders' Meeting of May 30, 2017, for a term of six years, i.e. until after the Shareholders' Meeting called to approve the financial statements for the year ending December 31, 2022.

It is no longer required to name an alternate when the auditor is a corporate entity; thus the two alternate auditors, Pierre Masieri and BEAS were not re-appointed at the 2017 Shareholders' Meeting.

5. Specific Controller

Fidus

26, rue Cambacérès – 75008 Paris

Represented by Jean-Michel Thierry, Partner

This appointment was re-appointed by the Supervisory Board on March 18, 2015, for a term of four years.

Alternate: Eric Lebègue

Appointed by the Supervisory Board on March 18, 2015, for a term of four years.

6. Information on elements likely to have a material impact in the event of a takeover or share exchange offer

Given that the Company's shares are not listed and that the securities (*obligations foncières*) it issues do not give access to its capital, there is no requirement to give specific information in relation to the provisions of article L.225-37-5 of the Code of Commerce. The composition of the share capital is specified below.

6.1 - INFORMATION ABOUT CAPITAL AND SHARES

6.1.1. Amount of capital; number and nature of the shares making up the capital

The Company's share capital currently stands at EUR 1,350,000,000, represented by 13,500,000 registered shares each with a face value of EUR 100. There are no other securities that give access to Caisse Française de Financement Local's capital.

6.1.2. Breakdown of capital

The capital of Caisse Française de Financement Local is owned by SFIL with the exception of one share which was lent to an individual (*prêt de consommation d'action*), a member of the Supervisory Board.

6.2 - INFORMATION CONCERNING VOTING RIGHTS (ARTICLE 31 OF THE BY-LAWS)

The voting rights attached to the shares are proportional to the percentage of capital those shares represent. Each share carries one voting right. At Shareholders' Meetings, the number of votes that may be cast by each shareholder corresponds to the number of shares held plus the number of shares for which the shareholder holds proxies.

6.3 - INFORMATION CONCERNING TRANSACTIONS BY EXECUTIVE OFFICERS ON THE COMPANY'S SHARES

No transaction is to be reported (cf. article 223-26 of the General Regulations of the Autorité des Marchés Financiers).

6.4 - CONVENTIONS SUBJECT TO ARTICLE L.225.37.4.2° OF THE CODE OF COMMERCE

No convention subject to article L.225.37.4.2° of the Code de Commerce requires mention.

IFRS Financial Statements

Assets

EUR millions	Note	12/31/2015	12/31/2016	12/31/2017
Central banks	2.1	2,496	3,684	1,706
Financial assets at fair value through profit or loss		2	-	-
Derivatives	4.1	7,043	6,437	4,629
Financial assets available for sale	2.2	889	1,736	2,048
Loans and advances due from banks	2.3	4,865	381	867
Loans and advances to customers	2.4	60,854	59,679	56,892
Fair value revaluation of portfolio hedge		2,784	3,053	2,518
Financial assets held to maturity		-	-	-
Current tax assets	2.5	0	0	0
Deferred tax assets	2.5	108	109	69
Accruals and other assets	2.6	20	28	48
TOTAL ASSETS		79,061	75,107	68,777

Liabilities

EUR millions	Note	12/31/2015	12/31/2016	12/31/2017
Central banks		-	-	-
Financial liabilities at fair value through profit or loss		2	1	4
Derivatives	4.1	12,013	9,800	7,930
Due to banks	3.1	5,520	5,225	4,821
Customer borrowings and deposits		-	-	-
Debt securities	3.2	57,142	56,110	52,898
Fair value revaluation of portfolio hedge		1,446	1,198	883
Current tax liabilities	3.3	1	0	0
Deferred tax liabilities	3.3	-	-	-
Accruals and other liabilities	3.4	1,584	1,424	823
Provisions	3.5	38	38	41
Subordinated debt		-	-	-
Equity		1,315	1,311	1,377
Capital and related reserve		1,315	1,315	1,350
Reserves and retained earnings		189	113	89
Gains and losses through equity		(113)	(127)	(103)
Net income		(76)	10	41
TOTAL LIABILITIES		79,061	75,107	68,777

Income statement

EUR millions	Note	2015	2016	2017
Interest income	5.1	4,047	3,256	2,645
Interest expense	5.1	(3,932)	(3,106)	(2,460)
Fee and commission income	5.2	0	0	3
Fee and commission expense	5.2	(26)	(7)	(15)
Net result of financial instruments at fair value through profit or loss	5.3	(32)	(38)	(33)
Net result of financial assets	5.4	(2)	14	16
Other income		0	0	0
Other expense		(0)	(0)	(0)
NET BANKING INCOME		55	119	156
Operating expense	5.5	(96)	(98)	(105)
GROSS OPERATING INCOME		(41)	21	51
Cost of risk	5.6	(14)	18	22
OPERATING INCOME		(55)	39	73
Net gains (losses) on other assets		-	-	-
INCOME BEFORE TAX		(55)	39	73
Income tax	5.7	(21)	(29)	(32)
NET INCOME		(76)	10	41
Earnings per share (in EUR)				
- Basic		(5.79)	0.76	3.07
- Diluted		(5.79)	0.76	3.07

Net income and unrealized or deferred gains and losses through equity

EUR millions	2015	2016	2017
Net income	(76)	10	41
Items that could be reclassified subsequently to profit or loss	34	(14)	24
Unrealized or deferred gains and losses of financial assets available for sale	49	(26)	32
Unrealized or deferred gains and losses of cash flow hedges	4	4	5
Taxes on items reclassified subsequently to profit or loss	(19)	8	(13)
Items that will not be reclassified subsequently to profit or loss	-	-	-
Total of unrealized or deferred gains and losses through equity	34	(14)	24
NET INCOME AND GAINS AND LOSSES THROUGH EQUITY	(42)	(4)	65

Equity

(EUR millions)	Capital and reserves			Unrealized or deferred gains and losses			Total equity
	Share capital, additional paid-in capital	Retained earnings and net income for the period	Total	Net change in fair value of available-for-sale financial assets, after tax	Net change in fair value of hedging derivatives, after tax	Total	
EQUITY AS OF DECEMBER 31, 2016	1,315	123	1,438	(104)	(23)	(127)	1,311
Shares issued	35	-	35	-	-	-	35
Dividends	-	(35)	(35)	-	-	-	(35)
Changes in fair value of available-for-sale financial assets through equity	-	-	-	20	-	20	20
Changes in fair value of derivatives through equity	-	-	-	-	4	4	4
Changes in fair value of available-for-sale financial assets through profit and loss	-	-	-	-	-	-	-
Changes in fair value of derivatives through profit and loss	-	-	-	-	-	-	-
Net income for the period	-	41	41	-	-	-	41
Other movements	-	-	-	-	-	-	-
EQUITY AS OF DECEMBER 31, 2017	1,350	130	1,480	(84)	(19)	(103)	1,377

The Ordinary Shareholder's meeting decided on May 30, 2017, to distribute a dividend in the amount of EUR 35 million. Each share (13,150,000 shares) received a dividend of EUR 2.67.

The Extraordinary Shareholder's meeting decided on May 30, 2017, to approve a capital increase in the amount of EUR 35 millions, thus increasing the share capital from EUR 1,315 million to 1,350 million.

Share capital currently stands at EUR 1,350,000,000 represented by 13,500,000 nominative shares.

Management Report

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IFRS Financial Statements

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Supplemental Disclosures

Shareholders' Meeting

General Information

Cash flow statement

EUR millions	2015	2016	2017
NET INCOME BEFORE TAXES	(55)	39	73
+/- Depreciation and write-downs	39	(23)	(56)
+/- Expense/income from investing activities	290	121	124
+/- Expense/income from financing activities	(184)	(59)	(99)
+/- Other items	102	315	24
= Non-monetary items included in net income before tax and other adjustments	247	354	(7)
+/- Cash from interbank operations	1,158	4,177	(883)
+/- Cash from customer operations	(772)	(961)	620
+/- Cash from financing assets and liabilities	3,222	(520)	313
+/- Cash from non-financing assets and liabilities	(1,258)	(731)	(607)
- Income tax paid	(35)	(17)	(29)
= Decrease/(increase) in cash from operating activities	2,315	1,948	(586)
CASH FLOW FROM OPERATING ACTIVITIES (A)	2,507	2,341	(520)
CASH FLOW FROM INVESTING ACTIVITIES (B)	-	-	-
+/- Cash from or for shareholders	-	-	(0)
+/- Other cash from financing activities	(540)	(1,148)	(1,452)
CASH FLOW FROM FINANCING ACTIVITIES (C)⁽¹⁾	(540)	(1,148)	(1,452)
EFFECT OF CHANGES IN EXCHANGE RATES ON CASH (D)	-	-	-
Increase/decrease in cash equivalents (A + B + C + D)	1,967	1,193	(1,972)
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	533	2,500	3,693
Cash and balances with central banks (assets & liabilities)	519	2,496	3,684
Interbank accounts (assets & liabilities) and loans/deposits at sight	14	4	9
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	2,500	3,693	1,721
Cash and balances with central banks (assets & liabilities)	2,496	3,684	1,706
Interbank accounts (assets & liabilities) and loans/deposits at sight	4	9	15
NET CHANGE IN CASH	1,967	1,193	(1,972)

(1) In 2017, the net cash flow of EUR -1.5 billion linked to financing activities corresponded to the change in debt represented by a security. Compared with the variation of EUR 3.2 billion in debt represented by a security mentioned in note 3.2.1., the difference primarily reflects the change in the revaluation of hedged risk and foreign exchange variations.

Notes to the IFRS financial statements

1. Accounting policies and valuation methods

1.1. CONTEXT OF PUBLICATION

Caisse Française de Financement Local decided to publish a set of individual financial statements according to IFRS, as adopted by the European Union. This publication is voluntary. The financial statements as of December 31, 2017, were examined by the Executive Board on March 26, 2018.

1.2. APPLICABLE ACCOUNTING STANDARDS

1.2.1. Application of IFRS as adopted by the European Union

On July 19, 2002, the European Union published regulation EC 1606/2002, which obliged listed groups to apply IFRS as from January 1, 2005. Caisse Française de Financement Local deliberately decided to apply all the IAS, IFRS, SIC and IFRIC adopted by the European Union as from January 1, 2007.

Since its publication in 2002, regulation EC 1606/2002 has been updated several times. Caisse Française de Financement Local's financial statements are prepared in accordance with all IFRS as adopted and endorsed by and applicable within the European Union.

The financial statements are prepared on a going-concern basis. They are stated in millions of euros (EUR) unless otherwise specified.

The preparation of financial information requires management to resort to estimates and assumptions that affect the amounts reported. In order to make these assumptions and estimates, management uses the information available at the date of preparation of the financial statements and exercises its judgment. While management believes it has considered all available information when making these assumptions, actual results may differ from such estimates and the differences may have a material impact on the financial statements.

Judgments were principally made in the following areas:

- classification of financial instruments;
- determination of whether or not the market is active for financial instruments measured at fair value;
- hedge accounting;
- existence of a present obligation with probable outflows in the event of litigation;
- identification of impairment triggers.

These judgments are detailed in the corresponding sections of these applicable accounting standards.

Estimates were principally made in the following areas:

- determination of fair value for financial instruments measured at fair value;
- determination of the recoverable amount of impaired financial assets;
- estimate of future taxable profit for the recognition and measurement of deferred tax assets.

Applying AMF Recommendation (DOC-2017-09) and ESMA Recommendation (ESMA32-63-340) issued on October 27, 2017, Caisse Française de Financement Local hereby confirms that the decision of the United Kingdom to leave the European Union ("Brexit") has no material impact on its financial statements as of December 31, 2017. Moreover, no material impact of such decision on the financial statements of Caisse Française de Financement Local during the next reporting periods has been foreseen.

1.2.2. Changes in accounting standards since the previous annual report that may impact Caisse Française de Financement Local

The following review of changes in accounting standards is based on the situation as of December 31, 2017.

1.2.2.1. IASB and IFRIC texts endorsed by the European Union and effective as of January 1, 2017

- **Amendment to IAS 12 Income taxes:** endorsed by the European Union on November 6, 2017 (Regulation EU n° 2017/1989) and effective for reporting periods beginning on or after January 1, 2017, this amendment intends to clarify how to assess under IAS 12 the recoverability of deductible temporary differences generated by unrealized losses on assets measured at fair value in the financial statements and at cost for tax purposes.

This amendment has no impact on Caisse Française de Financement Local's accounting treatment of deferred tax assets given that Caisse Française de Financement Local's methodology was already in line with the clarifications made by the amendment. Deferred tax assets are actually regularly reviewed and taxable results projections enable to ensure they can

be utilized against future taxable profits in a reasonable time horizon. In addition, Caisse Française de Financement Local takes into account the limitations possibly imposed by tax authorities regarding the origins of taxable profit against which deductible temporary differences can be utilized. Finally it shall be noticed that Caisse Française de Financement Local is within the exclusive authority of the French tax authorities.

- **Amendment to IAS 7 Cash-flow statements:** endorsed by the European Union on November 6, 2017 (Regulation EU n° 2017/1990) and effective for reporting periods beginning on or after January 1, 2017, this amendment intends to give more insights on the variation of the debt related to financing activities by breaking it down into two kinds of variations: cash-flow related variations (to be put in perspective with cash-flow statements) and other variations (perimeter variations, foreign exchange fluctuation impact, fair-value variation, etc.).

So as to comply with this amendment, additional pieces of information have been inserted at the bottom of cash-flow statements; they are linked with the variation of some aggregate balances of the balance sheet.

1.2.2.2. IASB and IFRIC texts endorsed by the European Union but not yet applicable

- **IFRS 9 Financial Instruments:** This standard, which will replace IAS 39, was adopted by the European Union on November 22, 2016 (Regulation EU n°2016/2067), and will come into effect for fiscal years beginning on or after January 1, 2018. It sets out new principles for:
 - classification and valuation of financial assets: accounting will be defined on the basis of the management model implemented, on the one hand, and the nature of the flows received, i.e. consisting exclusively of payments of principal and interest (SPPI⁽¹⁾), or including other elements (non-SPPI), on the other hand;
 - impairment for credit risk: the standard introduces a single loss impairment model that requires to account for 12-month expected credit losses for all assets that enter into the balance sheet, and lifetime expected credit losses if the credit risk increased significantly since the initial recognition of the asset;
 - hedge accounting, with the exception of macro-hedging transactions, which are to be the subject of a separate draft standard currently being studied by the IASB.

As for financial instruments recorded as liabilities on the balance sheet, the only change is the recognition of changes in fair value of one's own credit risk, for financial liabilities designated at fair value (fair value option). They will be recorded in shareholders' equity without any subsequent recycling in profit or loss.

Classification and Measurement

The management model implemented by Caisse Française de Financement Local has been formalized for the different portfolios of financial assets:

- the management model implemented for all loan portfolios and most of securities portfolios is the Hold-To-Collect model: such assets will be accounted for and measured at amortized cost except the ones which do not meet the cash flow criterion representing solely principal and interests;
- only securities held for cash investment purposes, which amount to approximately 2% of the overall outstanding securities as of December 31, 2017, may if appropriate be classified within an Hold-To-Collect-and-Sale management model: this comes from the higher sales frequency and volume for these assets, objective of which is specifically to address day-to-day liquidity management needs of Caisse Française de Financement Local. These assets shall be accounted for and measured at fair value through other comprehensive income.

Some loans, which do not meet the cash flow criterion representing solely principal and interests and represent less than 15% of non-derivative financial instruments held in the balance sheet, shall be accounted for and measured at fair value through profit or loss. Such measurement will be performed according to a mark-to-model-based methodology due to the absence of observable prices in an active market.

Furthermore, the policy implemented by Caisse Française de Financement Local from its creation to reduce loan sensitivity resulted in the transformation of a large number of loans with a structured (non-SPPI) component into fixed or variable rate loans (SPPI). These transactions did not give rise to derecognition of the initial assets under IAS 39, as the financial conditions of the new loan comply with the principle of IAS 39 AG62. However, under IFRS 9, the terms of the restructured transaction are substantially different, as there is a change in the SPPI criterion, which is a key factor for the definition of the applicable accounting treatment. Since the application of the standard is retroactive, Caisse Française de Financement Local has therefore determined the impacts that would have resulted from derecognition of financial instruments on the date of the transformation. The corresponding impact (adjusted for the time-related amortization) will be recorded as a counterpart to equity on the date of first application of the standard.

Moreover, on October 12, 2017, IASB issued an amendment to IFRS 9 entitled "Prepayment Features with Negative Compensation" which deals with instruments whose contractual terms may eventually result in a prepayment inferior to the sum of the outstanding principal and accrued interest. Under this amendment, such instruments do meet the SPPI criterion, provided that the prepayment essentially represents the outstanding principal and the related interest plus a reasonable compensation irrespective of its sign (payment by the borrower to the lender or by the lender to the borrower). Effective for reporting periods beginning on or after January 1, 2019, an earlier application of this amendment is permitted. Caisse Française de Financement Local opted for an earlier application of this amendment, given on the one hand the recommendation for endorsement issued in November 2017 by EFRAG, and on the other hand the support expressed by the Autorité des Marchés Financiers for an earlier application when such application enhance consistency and continuity in the application of accounting principles.

(1) SPPI: Solely Payments of Principal and Interest

Finally, as above mentioned, some securities which were or had been accounted for in a portfolio of assets available for sale under IAS 39, shall be now accounted for at amortized cost under IFRS 9: as for the first time application impact, the accounting change results in the reclassification in 2018 opening equity of the unrealized gain or losses accumulated in equity up to December 31, 2017.

Impairment of Financial Assets

As required under IFRS 9, the Company has defined the set of rules to break down its exposure into three categories, "buckets", depending on credit quality evolution since initial recognition. This set of rules relies on the existing risk monitoring framework of processes and committees (Watchlist Committee, Default Committee).

The Standard also requires to define forward-looking scenarios in the objective of prospectively determining expected credit losses.

The Company has leveraged on its existing framework of calculation of the capital requirements involved by credit risk pursuant to Prudential Regulation (advanced models and prudential calculation rules) and, in the prospect of integrating a prospective dimension, forward-looking scenarios (projections of financial information impacting the portfolios) have been taken into consideration.

For bucket 1 and bucket 2 assets, the Expected Credit Losses calculation under IFRS 9 is inspired by the Expected Loss calculation under Basel Committee rules (use of Exposure at Default, Probability of Default and Loss Given Default parameters and discounting at the effective interest rate). For bucket 3 assets, the Expected Credit Losses calculation is based mainly on individual recovery hypotheses made by the Credit Risk Department.

Finally, as regards the prudential requirements, Caisse Française de Financement Local will not apply the phase-in provisions embedded within Regulation EU n° 2017/2395 regarding the first time application impact of the standard.

Hedge accounting

In the case of hedge accounting, the standard leaves the choice, when first applying IFRS 9, to apply the new provisions or to maintain the provisions in force under IAS 39 until the entry into force of the future macro-hedging standard. Caisse Française de Financement Local has decided to maintain the provisions of IAS 39 for hedge accounting at the date of entry into force of IFRS 9. However, the Company will publish the financial information on hedge accounting that is required as a result of the amendments to IFRS 7 Financial Instruments: Disclosures.

Implementation of IFRS 9

The implementation of the new standard is based on a steering committee involving executive management, the finance division, the risks division, the head of information systems, as well as the president of the executive board of Caisse Française de Financement Local.

Work on changes to the information systems related to this new standard has been integrated into the work plan and planning of the business teams and IT teams for 2017. All the components of the information system affected by the implementation of IFRS 9 are subject to tests which are partly integrated into the IT simplification and reinforcement program.

The governance of Caisse Française de Financement Local has been adapted so as to integrate the elements relating to the new standard into the existing procedures: Asset-Liability Management Committee will be in charge of determining and monitoring the management model pursued while New Product Committee will be in charge of assessing whether products meet the SPPI criterion.

Politics and procedures embedded within the existing risk management framework (watchlist and defaults) have been reviewed and updated through the inclusion of *ad hoc* documents, with the purpose of addressing the issue of impairment under IFRS 9.

Similarly, methodologies (models and parameters used), forward-looking scenarios and likelihood of occurrence related to impairment under IFRS 9 have been validated by the department credit validation and quality control. These scenarios are embedded within the formal reporting sent to Credit Validation Committee and then to Risk Committee and the Risk and Internal Control Committee, the latter being a specialized committee of the SFIL's Board of Directors.

Moreover, backtesting procedures have been defined in order to monitor on an annual basis the efficiency of the framework of Expected Credit Loss calculation under IFRS 9; such procedures encompass the assessment of data quality, portfolio structure and forecast accuracy.

On each balance sheet date, the split in buckets as well as the impairment amounts are submitted for assessment and approbation to the Impairment Committee prior to their integration in the information systems. Impairment amounts are disclosed both internally - through a quarterly presentation to the Risk and Internal Control Committee with the Quarterly Risk Review - and externally - through financial reports.

Finally, the Financial Statements Committee of the Company, which is an emanation of the SFIL's Board of Directors, the Executive Board and the Supervisory Board of Caisse Française de Financement Local have been regularly informed on IFRS 9 project progress and on the financial impacts of the entry into force of this new standard.

Amendments of IFRS framework induced by IFRS 9

IFRS 9 amends some other IFRS, in particular:

- IAS 1 Presentation of financial statements: the accounting headings belonging to Net banking income and other comprehensive income are modified and adapted to IFRS 9;
- IFRS 7 Financial Instruments: Disclosures: additional pieces of information in Annex are required, especially relating to hedge accounting.

- **Amendment to IFRS 15 Revenue from contracts with customers:** endorsed by the European Union on September 22, 2016 (Regulation EU n° 2016/1905), and effective for reporting periods beginning on or after January 1, 2018, this standard deals with contracts with customers, excluding financial instruments, insurance contracts and leases.

Contracts concluded by Caisse Française de Financement Local are out of the scope of this standard.

- **Amendment to IFRS 16 Leases:** endorsed by the European Union on October 31, 2017 (Regulation EU n° 2017/1986) and effective for reporting periods beginning on or after January 1, 2019, this standard, which will eventually replace IAS 17, states that at the commencement date a lessee shall recognize both a right-of-use asset and a lease liability.

The impacts of this standard on the financial statements of Caisse Française de Financement Local are being analyzed. The calculation of IFRS 16 first time application impact is being performed and, applying IFRS 16.C5.(b), Caisse Française de Financement Local moves towards the limited restatement method. Caisse Française de Financement Local has not opted for an earlier application of this new standard.

1.3. ACCOUNTING PRINCIPLES APPLIED TO THE FINANCIAL STATEMENTS

1.3.1. Offsetting financial assets and financial liabilities

Financial assets and financial liabilities are offset and the net amount is reported in the balance sheet when there is a legally enforceable right to set off the recognized amounts and there is an intention for both parties to settle expected future cash flows on a net basis or to realize the asset and settle the liability simultaneously.

1.3.2. Foreign currency transactions

Foreign currency transactions are accounted for using the exchange rate prevailing on the transaction date. Monetary assets and liabilities denominated in foreign currencies are recognized at closing rates. Non-monetary assets and liabilities recognized at fair value and denominated in foreign currencies existing at the closing date are recorded at closing rates, whereas non-monetary assets and liabilities recognized at amortized cost are recorded at their historical rates.

Any resulting exchange differences from monetary assets and liabilities are recognized in the income statement, except for the foreign exchange impact of fair value adjustments on available for sale assets, which are recognized in equity. Foreign exchange differences from non-monetary assets and liabilities recognized at fair value are recorded as fair value adjustments.

1.3.3. Trade date and settlement date accounting

All purchases and sales of financial assets are recognized on settlement date, which is the date that a financial asset is received or delivered by Caisse Française de Financement Local. Hedging instruments are recognized at fair value on the transaction date.

1.3.4. Financial assets

Management determines the appropriate classification of its investments at initial recognition. However, under certain conditions financial assets may be subsequently reclassified.

1.3.4.1. Loans and advances to banks and customers

Loans are defined as non-derivative financial assets with fixed or determinable payments that are not listed on an active market, other than:

- those that the entity intends to sell immediately or in the near future, which should be classified as held for trading, and those that the entity, upon initial recognition, designates at fair value through profit or loss;
- those that the entity, upon initial recognition, designates as available for sale; or
- those for which the holder may not recover substantially all of the initial investment for reasons other than the deterioration of credit, which should be classified as available for sale.

Caisse Française de Financement Local recognizes loans and advances initially at fair value plus any directly attributable transaction costs. Subsequent measurements are made at amortized cost, less any impairment. Interest is recognized in net interest income based on the effective interest rate method.

The effective interest rate is the rate that accurately discounts the expected future cash flows over the life of the financial instrument or, where more appropriate, over a shorter period, so as to obtain the net carrying amount of the financial asset.

The calculation of this rate takes into account the commissions received or paid which, because of their nature, form an integral part of the effective rate of the contract, transaction costs and possible premiums and discounts.

1.3.4.2. Financial assets held to maturity

Caisse Française de Financement Local holds no assets held to maturity.

1.3.4.3. Financial assets available for sale

Assets intended to be held for an indefinite period of time and which may be sold in response to a need for liquidity or changes in interest rates, exchange rates or equity prices are classified as Financial assets available for sale.

Available-for-sale assets are initially recognized at fair value (including transaction costs). Interest on fixed-income securities is recognized based on the effective interest rate method in the interest margin. Dividends received on variable-income securities are recorded in Net gains (losses) on financial assets available for sale.

Unrealized gains and losses arising from changes in the fair value of available-for-sale financial assets are recognized in equity. When assets are disposed of, the related accumulated fair value adjustments are reversed in the income statement in Net gains (losses) on financial assets available for sale.

On October 1, 2008, available-for-sale financial assets have been restated as Loans and advances at a later date. On the basis of the October 2008 amendment to IAS 39, the reserve representative of changes in the fair value of available-for-sale financial assets as presented in the financial statements as of December 31, 2017, corresponds to the part of this reserve still to be amortized with regard to the securities restated as of October 1, 2008, and which had been frozen on that date.

1.3.4.4. Financial assets held for trading

Caisse Française de Financement Local holds no assets for trading purposes.

1.3.4.5. Financial assets designated at fair value through profit or loss

Caisse Française de Financement Local does not use the option to designate its financial assets at fair value through profit or loss.

1.3.4.6. Realized gains and losses on sales of financial assets

For financial assets measured at amortized cost, realized gains and losses on disposals are the differences between the proceeds received (net of transaction costs) and the carrying amount of the assets. The carrying amount is systematically determined based on the "first in, first out" approach.

When an available-for-sale financial asset is sold, the total of gains and losses previously recognized in equity is reversed in profit and loss.

1.3.4.7. Early reimbursement indemnities

Caisse Française de Financement Local has determined the accounting principles applicable to the restructuring of loans in accordance with AG 62 of IAS 39 concerning financial liabilities.

Several possibilities are considered depending on whether the early reimbursement is recognized as being an early reimbursement with refinancing or without refinancing.

Early reimbursement with refinancing

The method of accounting for early reimbursement indemnities differs depending on whether the restructuring conditions are substantially different from those set initially.

In line with the principles of AG 62 of IAS 39, Caisse Française de Financement Local considers that the conditions are substantially different when the net present value of the cash flows under the new conditions, including any fees paid net of any fees received, is more than 10% different from the net present value of the cash flows remaining from the original loan.

If the difference in net present value is less than 10%, any early reimbursement indemnities are amortized over the term of the new loan as there is continuity between the two operations. If the difference exceeds 10%, early reimbursement indemnities are recognized directly in income of the related period.

Early reimbursement without refinancing

When a loan has been extinguished, Caisse Française de Financement Local recognizes early reimbursement indemnities and any gains or losses of unamortized premium or discount, as income for the period.

1.3.4.8. Impairment of financial assets

Caisse Française de Financement Local records allowances for impairment losses when there is objective evidence that a financial asset or group of financial assets is impaired. Impairment results from one or more loss events occurring since initial recognition and when that loss event has an impact on the estimated future cash flows that can be reliably estimated. The impairment represents the management's best estimate of losses in the value of assets at each reporting date.

Financial assets at amortized cost

Caisse Française de Financement Local first assesses whether objective evidence of impairment exists for a financial asset when taken individually. If no such evidence exists, the financial asset is included in a group of financial assets with similar credit risk characteristics and collectively assessed for impairment.

- **Determination of impairment**

- **Specific impairment:** if there is objective evidence that loans or other receivables, or financial assets classified as held-to-maturity are impaired, the amount of the provision is calculated as the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, net of any guarantees and collateral, discounted at the financial instrument's original effective interest rate (except for reclassified assets, see below). When an asset is assessed as being individually impaired, it is excluded from the portfolio on which collective impairment is calculated. As from the impairment of the asset, the Interest income section of the income statement records the theoretical remuneration of the asset calculated by applying the original effective interest rate to the net book value of impairment.
- **Collective impairment:** collective impairment covers the risk of loss in value not covered by specific impairment where there is objective evidence that probable losses are present in certain segments of the portfolio or other lending commitments at the balance sheet date. These losses are estimated on the basis of past performance and historical patterns of losses in each segment and the current economic environment in which the borrowers operates. For this purpose, Caisse Française de Financement Local uses a credit risk model based on an approach that combines default probabilities and losses in the event of default. This model is subject to regular back-testing and is based on Basel III data and risk models, consistent with the incurred loss model.

- **Accounting treatment of impairment**

Changes in the amount of impairment losses are recognized in the income statement as Cost of risk. Once an asset has been written down, if the amount of the impairment subsequently decreases due to an event occurring after recognition of the impairment, the write-back of the impairment is credited to the Cost of risk.

When an asset is determined by management as being irrecoverable, the outstanding specific impairment is reversed via the income statement, in Cost of risk and the net loss is recorded under the same heading. Subsequent recoveries are also recognized as Cost of risk.

Reclassified financial assets

Reclassified financial assets are impaired following the same rules as financial assets measured at amortized cost. If there is objective evidence that reclassified financial assets are impaired, the amount of the impairment on reclassified assets is calculated as the difference between the net carrying amount of the asset and the net present value of the expected cash flows discounted at the effective interest rate at the time of reclassification. Any existing unamortized reserve of unrealized gains and losses will be taken to the profit or loss account in Cost of risk.

In the event of a positive update to expected cash flows, the impairment amount is reversed through the interest margin over the new schedule of expected cash flows, not by a reversal of impairment in Cost of risk.

Financial assets available for sale

Impairment of available-for-sale financial assets is recognized on an individual basis if there is objective evidence of impairment as a result of one or more events occurring since initial recognition of the asset. These assets are subject only to specific impairment.

- **Determination of impairment**

Financial assets available for sale held by Caisse Française de Financement Local are only debt securities. For the latter, impairment is triggered based on the same criteria as those applied to financial assets valued at amortized cost (see above).

- **Accounting treatment of impairment**

When financial assets available for sale are impaired, the total reserve in other comprehensive income is recycled into profit or loss and Caisse Française de Financement Local reports these impairment losses in the income statement in Cost of risk (when the financial asset available for sale is with fixed income) or in Gains (losses) in Net banking income (when the financial asset is with variable income). Any subsequent decline in fair value constitutes an additional impairment loss, recognized in the income statement.

In the event of an increase in the fair value of financial asset available for sale that relates objectively to an event occurring after the last impairment was recognized, Caisse Française de Financement Local recognizes a reversal of the impairment loss in the income statement in Cost of risk when the asset is with fixed income.

Off-balance sheet commitments

Off-balance sheet commitments such as credit substitutes (e.g. guarantees and standby letters of credit) and loan commitments are converted into on-balance sheet items when called. However, under specified circumstances such as uncertainty about the counterparty's creditworthiness, the off-balance sheet commitment should be classified as impaired if the credit worthiness has deteriorated to an extent that makes the payment of principal and interest uncertain.

1.3.4.9. Sale and repurchase agreements and lending of securities

Securities sold subject to a linked repurchase agreement at a predetermined price (repo) are not derecognized and remain on the balance sheet in their original category. The corresponding liability is included in Customer borrowings and deposits or Due to banks, as appropriate. The asset is reported as pledged in the notes.

Securities purchased under an agreement to resell at a predetermined price (reverse repo) are recorded as off-balance sheet items and the corresponding loans are recorded in Loans and advances to customers or Loans and advances due from banks, as appropriate.

The difference between the sale and repurchase price is recognized as interest income or expense and is amortized over the life of the agreement using the effective interest rate method.

Securities lent to third parties are retained in the financial statements. Securities borrowed are not recognized in the financial statements. If these borrowed securities are sold to third parties, the obligation to return them is recorded at fair value in Financial liabilities at fair value through profit or loss, and the gain or loss is included in Net gains (losses) on financial instruments at fair value through profit or loss.

1.3.5. Financial liabilities

1.3.5.1. Financial liabilities designated at fair value through profit and loss

Caisse Française de Financement Local does not use this option.

1.3.5.2. Financial liabilities at amortized cost

Financial liabilities at amortized cost are recognized initially at fair value, being their issue proceeds net of transaction costs incurred. They are subsequently recognized at amortized cost and any difference between their initial carrying amount and the redemption value is recognized in the income statement over the period of the borrowings using the effective interest rate method.

Financial liabilities at amortized cost are mainly *obligations foncières* and other resources benefiting from the privilege defined in article L.513-11 of the Monetary and Financial Code.

Obligations foncières are recorded at nominal value. Reimbursement premiums and issue premiums are amortized according to a quasi-actuarial method over the life of the securities concerned, as of the first year, *prorata temporis*. They are recorded on the balance sheet in items corresponding to the type of debt concerned. The amortization of these premiums is recorded in the income statement as Interest income and expense on debt securities. In the case of bonds issued above par, the amortization of issue premiums is deducted from related interest income and expense on debt securities.

Interest related to *obligations foncières* is accounted for in interest margin as Interest expense for accrued amounts, due and not yet due, calculated *prorata temporis* on the basis of contractual rates.

Fees and commissions on bond issues are amortized according to a quasi-actuarial method over the life of the bonds to which they are attached and are accounted for in interest margin as Interest expense.

Bonds denominated in other currencies are treated in the same way as foreign currency transactions (see above Foreign currency transactions).

Registered covered bonds are private placements recorded at nominal value. Related issue premiums and interest are dealt with in the same way as *obligations foncières* (see above).

1.3.6. Derivatives

All derivatives are initially recognized on the balance sheet at fair value and then are revalued at their fair value. The fair value of derivatives is calculated either on the basis of prices observed in listed markets or by using internal valuation models.

The amount registered on the balance sheet includes the premium paid or received after amortization, the amount of changes in fair value and accrued interest, which altogether make up the fair value of the derivative. Derivative instruments are recorded in the assets if their fair value is positive and in the liabilities if it is negative.

1.3.6.1. Derivatives not used in a hedging relationship

Caisse Française de Financement Local is only authorized to enter in derivative transactions for hedging purposes. These derivatives are usually documented in a hedging relationship.

- Nevertheless, as of December 31, 2017, some derivatives could not be recorded as such; that resulted:
- either from operations in which hedge effectiveness tests failed after the hedged items were impaired;
- or from derivatives that hedge the foreign exchange risk related to export credit financing loans denominated in a currency other than the euro, and that are concluded before the end of the drawing phase of the hedged loans. At this stage, hedging of currency risk relating to monetary assets or liabilities has been documented only from the complete payment

in the entity's balance sheet. The adaptation of this documentation should make possible the qualification of these derivatives in accounting hedging from January 1, 2018.

Both realized and unrealized gains and losses are recognized in Net result of financial instruments at fair value through profit or loss.

1.3.6.2. Hedging derivatives

Hedging derivatives can be categorized as either:

- hedges of the fair value of a recognized asset or liability or a firm commitment (fair value hedge); or
- hedges of a future cash flow that might eventually impact the future income statement and that is attributable to a recognized asset or liability or a forecast and highly probable future transaction (cash flow hedge).

Hedge accounting may be used for such derivatives, provided certain criteria are met:

- formal documentation of the hedging instrument, hedged item, hedging objective, strategy and relationship between the hedging instrument and the hedged item must be prepared before hedge accounting is applied;
- the hedging relationship is expected to be effective both prospectively and retrospectively in offsetting changes in fair value or cash flows attributable to the hedged risk on the hedged item throughout the reporting period;
- the hedge, effectiveness of which has been reliably measured, shall be effective at inception and on an ongoing basis;
- for hedges of a future cash flow, the future transaction that constitutes the hedged item must be highly probable and must involve an exposure to variations in cash flows that could ultimately affect the income statement.

Changes in the fair value of derivatives that are designated and documented in a fair value hedging relationship, and that respect the criteria set out above, are recorded in the income statement, along with the corresponding change in fair value of the hedged assets or liabilities which are attributable to that specific hedged risk.

Regarding notably structured financial instruments, the existence of a perfect hedge with a derivative, and the documentation of the associated hedging relationship, have the effect of re-evaluating the hedged risk of the financial instrument, in parallel with the revaluation of the hedging derivative. This results in the same accounting effects as if the derivative embedded in the financial instrument has been separated.

If at any time the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged interest-bearing financial instrument is amortized to profit or loss over the residual maturity of the hedged item by adjusting the yield on the hedged item.

The effective portion of the changes in the fair value of derivatives that are designated in a cash-flow hedging relationship, that respect the criteria set out above, and that prove to be effective in relation to the hedged risk, is recognized in equity as Unrealized or deferred gains and losses of cash-flow hedges. The non-effective portion of the changes in the fair value of the derivatives is recognized in the income statement. Amounts deferred in equity are transferred to the income statement and classified as income or expense in the periods during which the hedged firm commitment or forecast transaction affect the income statement.

1.3.6.3. Hedging of the interest rate risk of a portfolio

Caisse Française de Financement Local makes use of the provisions of IAS 39 as adopted by the European Union (IAS 39 carve-out) because it better reflects the way Caisse Française de Financement Local manages its financial instruments.

The objective of hedging relationships is to reduce the interest rate risk exposure stemming from certain categories of assets or liabilities designated as the qualifying hedged items.

The entity performs a comprehensive analysis of its interest rate risk exposure. It consists in assessing fixed rate exposure generated by all fixed-rate balance sheet items. Caisse Française de Financement Local selects financial assets and liabilities to be included in the hedge of the portfolio's interest rate risk exposure. The entity constantly applies the same methodology for selecting financial assets and liabilities to be included in the portfolio. The financial assets and liabilities are classified by time-buckets. Hence, when they are removed from the portfolio, they must be removed from all the time-buckets on which they have an impact.

The Company chose to put together homogeneous portfolios of loans and portfolios of bond issues. Based on this gap analysis, which is realized on a net basis, Caisse Française de Financement Local defines at inception the risk exposure to be hedged, the length of the time-buckets and the manner and the frequency of testing.

The hedging instruments are portfolios of derivatives, whose positions may be offsetting. The hedging items are recognized at their fair value (including accrued interest expense or income) with adjustments recorded in the income statement.

Revaluation related to the hedged risk is recognized in the balance sheet (in asset or liability depending on positive or negative revaluation) as Fair value revaluation of portfolio hedge.

1.3.7. Fair value of financial instruments

Fair value is 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, either in the principal market, or in its absence, in the most advantageous

market Caisse Française de Financement Local can access. The fair value of a liability reflects the effect of the risk of non-performance, which in particular includes Caisse Française de Financement Local's own credit risk.

Market prices are used to determine the fair value of financial assets and liabilities when there is an active market, defined as so by the existence of sufficient frequency and volume to provide pricing information on an ongoing basis. Active market prices are not, however, available for a significant number of the financial assets and liabilities held or issued by Caisse Française de Financement Local.

If a financial instrument is not listed in an active market, valuation techniques are used. Valuation techniques include the use of market data from recent arm's length transactions between knowledgeable, willing parties, reference to the current fair value of another instrument that is substantially the same, and valuation models.

A valuation model reflects what the transaction would have been under the market conditions existing on the measurement date. The valuation model should take into account all the factors that market participants would consider when pricing the asset, such as credit worthiness evolution and market liquidity. Within this framework, Caisse Française de Financement Local uses its own valuation models and market assumptions, i.e. present value of cash flows or any other techniques based on market conditions existing at the reporting date.

1.3.7.1. Financial instruments measured at amortized cost

The following remarks are applicable to the fair value of loans and advances presented in the notes:

- the fair value of fixed-rate loans is estimated by comparing market interest rates when the loans were granted with current market interest rates offered on similar loans;
- caps, floors and early repayment options are included in determining the fair value of loans and advances.

1.3.7.2. Financial instruments measured at fair value

Available-for-sale financial assets and derivatives are measured at fair value by reference to listed market prices when available. When listed market prices are not available, fair values are estimated on the basis of pricing models or discounted cash flows, using as much as possible observable, and if necessary non-observable, market data.

For available-for-sale financial assets, when listed prices are not available, the pricing models attempt to reflect as accurately as possible the market conditions on the valuation date as well as any changes in the credit quality of these financial instruments and the market liquidity.

To determine the fair value of its derivatives, Caisse Française de Financement Local uses different discounting curves in function of the effective exchange of collateral with its counterparty. When Caisse Française de Financement Local receives collateral, future derivative cash flows are discounted with an overnight indexed swap (OIS). On the other hand, when no collateral is exchanged, they are discounted with a Euribor-type curve. This differential treatment reflects the different financing cost associated with the derivatives used by the Company (FVA - *funding valuation adjustment*). As a reminder, Caisse Française de Financement Local does not pay collateral to its derivative counterparties, since they benefit from the legal privilege on assets for the same reason as holders of *obligations foncières*.

In addition, a valuation adjustment is taken into account in the valuation of derivatives to reflect the impact of a counterparty's credit risk (CVA - credit valuation adjustment) or the counterparty's net exposure to the credit risk of Caisse Française de Financement Local (DVA - debit valuation adjustment). This valuation adjustment makes it possible to switch from a fair value based on risk-free rate discounted cash flows, i.e. abstracting from the counterparty risk, to fair value that integrates this risk. It is determined in function of the exposure to risk combined with rates of losses integrating market parameters.

1.3.8. Interest income and expense

For all interest-bearing instruments that are not measured at fair value, interest income and expense are recognized in the income statement using the effective interest rate method (transaction cost being included).

The effective interest rate is the rate that exactly discounts expected future cash flows through the life of the financial instrument, or when appropriate, a shorter period to determine the net carrying amount of the financial asset. The calculation of this rate includes commissions received or paid that are an integral part of the effective interest rate due to their nature, transaction costs and any premiums and discounts.

Transaction costs are incremental costs that are directly attributable to the acquisition of a financial asset or liability and are used for the calculation of the effective interest rate. An incremental cost is one that would not have been incurred if the entity had not acquired the financial instrument.

Accrued interest is recognized on the balance sheet in the same item as the related financial asset or liability.

Once an interest-bearing financial asset has been written down to its estimated recoverable amount, interest income is thereafter recognized based on the effective interest rate used to discount the recoverable future cash flows.

1.3.9. Commission income and expense

Most of the commissions arising from Caisse Française de Financement Local's activities are recognized on an accrual basis over the life of the underlying transaction.

Loan commitment commissions are recognized as part of the effective interest rate if the loan is drawn. They are recorded as commission income on the expiry date of the commitment if no loan has been granted.

1.3.10. Deferred taxes

Deferred taxes are recognized using the liability method to account for temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. The tax rates enacted or substantively enacted at the reporting date are used to determine deferred taxes.

Deferred tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

Deferred tax liabilities are recognized to account for temporary differences arising from investments in subsidiaries, jointly controlled companies and associates, except where the timing of the reversal of the temporary difference cannot be controlled and it is probable that the difference will not reverse in the foreseeable future.

Deferred taxes related to fair value re-measurement of assets available for sale and cash flow hedges, and other operations charged or credited directly to other comprehensive income, are also credited or charged directly to other comprehensive income.

1.3.11. Provisions

Provisions are mainly for litigation, restructuring and off-balance sheet loan commitments.

A provision is measured at the present value of the expenditures expected to be required to settle the obligation. The discount rate used is the pre-tax rate that reflects current market assessments of the time value of money. Provisions are recognized when:

- Caisse Française de Financement Local has a present legal or constructive obligation as a result of past events;
- it is probable that an outflow of resources representing economic benefits will be required to settle the obligation;
- a reliable estimate of the amount of the obligation can be made.

Provisions on loan commitments are recognized using the method applied for the impairment of financial assets measured at amortized cost.

1.3.12. Earnings per share

Basic earnings per share before dilution are calculated by dividing net income available to shareholders by the weighted average number of ordinary shares in issue during the year.

1.3.13. Related-party transactions

Two parties are considered to be related if one has the ability to control the other party or exercise significant influence over the other party when making financial or operational decisions. The parent company of Caisse Française de Financement Local is SFIL, a *société anonyme* incorporated in France, which is owned by the French State, Caisse des Dépôts et Consignations and La Banque Postale, the last two also incorporated in France. Within this framework, related-party transactions are those with companies owned directly or indirectly by the same final shareholder and with directors.

1.3.14. Segment reporting

Caisse Française de Financement Local's sole activity is the financing or refinancing of commitments on public sector (loans to French local governments and public hospitals, or loans to SFIL with an unconditional and irrevocable 100% guarantee by the French State, as part of the financing of large export credits).

Caisse Française de Financement Local conducts its business solely from France. The Company has no direct activities in other countries and is unable to present a relevant breakdown of its results by geographic region.

1.3.15. Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with banks or central bank and interbank deposits at sight.

2. NOTES TO THE ASSETS (EUR millions)

2.1 - CENTRAL BANKS

	12/31/2015	12/31/2016	12/31/2017
Mandatory reserve deposits with central banks	-	-	-
Other deposits	2,496	3,684	1,706
TOTAL	2,496	3,684	1,706

2.2 - FINANCIAL ASSETS AVAILABLE FOR SALE

2.2.1. Analysis by nature

	12/31/2015	12/31/2016	12/31/2017
Loans	-	-	-
Bonds	889	1,736	2,048
TOTAL	889	1,736	2,048

2.2.2. Analysis by counterparty

	12/31/2015	12/31/2016	12/31/2017
Public sector	889	1,089	1,474
Credit institutions guaranteed by the public sector	-	-	-
Total public sector	889	1,089	1,474
Credit institutions	-	647	574
Total replacement assets	-	647	574
TOTAL	889	1,736	2,048
<i>of which eligible for central bank refinancing</i>	<i>600</i>	<i>1,320</i>	<i>1,830</i>

2.2.3. Impairment

	12/31/2015	12/31/2016	12/31/2017
Public sector	889	1,089	1,474
Replacement assets	-	647	574
Total performing assets	889	1,736	2,048
Public sector	-	-	-
Replacement assets	-	-	-
Total impaired assets	-	-	-
Specific impairment	-	-	-
TOTAL ASSETS AFTER IMPAIRMENT	889	1,736	2,048

2.2.4. Analysis by residual maturity

See note 7.4

2.2.5. Unrealized or deferred gains and losses, breakdown by country

See note 4.4

2.3 - LOANS AND ADVANCES DUE FROM BANKS

2.3.1. Analysis by nature

	12/31/2015	12/31/2016	12/31/2017
Sight accounts	4	4	11
Other loans and advances due from banks	4,861	377	856
Performing assets	4,865	381	867
Impaired loans and advances	-	-	-
Impaired assets	-	-	-
Total assets before impairment	4,865	381	867
Specific impairment	-	-	-
Collective impairment	-	-	-
TOTAL	4,865	381	867

In 2016, the decrease of this item results from the maturity of a loan, guaranteed by loans to British local authorities, and from the early repayment of a loan to the parent company, SFIL.

2.3.2. Breakdown by counterparty

	12/31/2015	12/31/2016	12/31/2017
SFIL - loans to refinance large export credit guaranteed by the French state ⁽¹⁾	-	-	218
Replacement assets	2,345	4	371
Swiss cantonal banks benefiting from their cantons' legal guarantee	373	113	30
Banks guaranteed by a local government, crédits municipaux	58	33	22
Other credit institutions of which loans benefiting from the assignment in guarantee of refinanced public debt	2,089	231	226
TOTAL	4,865	381	867
<i>of which eligible for central bank refinancing</i>	-	-	-

(1) Caisse Française de Financement Local grants loans to its parent company, SFIL, to refinance large export credits it has granted. Such loans benefit from an irrevocable and unconditional 100% guarantee by the French State, referred to as an enhanced guarantee.

2.3.3. Replacement assets

	12/31/2015	12/31/2016	12/31/2017
SFIL - loans secured by public sector assets	2,341	-	-
SFIL - other loans non secured by public sector assets ⁽¹⁾	-	-	360
Sight accounts	4	4	11
TOTAL	2,345	4	371

(1) In 2017, Caisse Française de Financement Local invested some of its surplus cash in loans granted to its parent company SFIL.

2.3.4. Analysis by residual maturity

See note 7.4

2.3.5. Unrealized or deferred gains and losses, breakdown by country

See note 4.4

2.4 - LOANS AND ADVANCES TO CUSTOMERS

2.4.1. Analysis by counterparty

	12/31/2015	12/31/2016	12/31/2017
Loans to public sector	56,585	56,469	53,946
Loans guaranteed by public sector	3,725	2,759	2,441
Performing assets	60,310	59,228	56,387
Loans to public sector	673	557	558
Loans guaranteed by public sector	-	-	-
Impaired assets	673	557	558
Total assets before impairment	60,983	59,785	56,945
Specific impairment	(66)	(60)	(23)
Collective impairment	(63)	(46)	(30)
TOTAL	60,854	59,679	56,892
<i>of which eligible for central bank refinancing</i>	<i>39,227</i>	<i>39,122</i>	<i>39,575</i>

Impaired assets concern customers that represent an identified credit risk (non-performing loans as of December 31, 2017: EUR 526 million) and customers with unpaid loans corresponding to disagreement on the amount due (litigious loans as of December 31, 2017: EUR 32 million).

Within the framework of the successful policy to reduce the interest rate sensitivity in 2016 and the confirmation of legal decisions favorable to the bank, Caisse Française de Financement Local was able to hone, in a reasonable and prudent manner, the methods it uses to estimate the recoverability of flows of non-performing loans on its balance sheet. In particular, in order to account for the impact of the spread of payments. The implementation of this approach, which is in compliance with IFRS, makes it no longer systematically necessary to estimate the total amount of interest to account for hypotheses of future recovery. Thus, the net interest rate expense is improved through a recovery of provisions in the amount of EUR 31 million, recorded as of December 31, 2017.

Assets considered as forborne by Caisse Française de Financement Local concern exposures to loan contracts for which concessions have been granted in light of the borrower's financial difficulties (recognized or to come) that would not have been granted in other circumstances. These concessions may either be a waiver of a part of the debt, a rescheduling of the loan repayment; concessions can also be granted as a consequence of restructuring measures through an amendment to the loan contract; or a partial or full refinancing of the loan with a new contract, including for transactions aiming to reduce the sensitivity of the loan.

There were 211 forborne contracts as of December 31, 2017, with 108 borrowers, for a total of EUR 1,364 million.

2.4.2. Analysis by residual maturity

See note 7.4

2.4.3. Unrealised or deferred gains and losses breakdown by country

See note 4.4

2.5 - TAX ASSETS

	12/31/2015	12/31/2016	12/31/2017
Current income tax	-	-	-
Other taxes	0	0	0
Current tax assets	0	0	0
Deferred tax assets (see note 4.2)	108	109	69
TOTAL TAX ASSETS	108	109	69

Deferred tax assets were submitted to a recoverability test taking into account the business plans presented to the Supervisory Board according to realistic hypotheses. Deferred taxes as of December 31, 2017, are recoverable on the basis of this analysis within seven years by taking into account the tax rules governing the treatment of past deficits. As of December 31, 2017, Caisse Française de Financement Local has no deferred tax assets related to carry forward tax losses.

In 2017, Caisse Française de Financement Local took into account the legislative measures designed to reduce the corporate income tax rate to 25% as of 2022. As of December 31, 2017, Caisse Française de Financement Local reduced its deferred tax assets and recorded an expense of EUR 2 million.

2.6 - ACCRUALS AND OTHER ASSETS

	12/31/2015	12/31/2016	12/31/2017
Cash collateral paid	-	-	-
Other accounts receivable	-	0	1
Prepaid charges	0	0	2
Other assets	20	28	45
TOTAL ACCRUALS AND OTHER ASSETS	20	28	48

2.7 - RESTATEMENT OF FINANCIAL ASSETS (IAS 39 AMENDED)

	From Financial assets held for trading to Loans and advances (a)	From Financial assets held for trading to Financial assets available for sale (b)	From Financial assets available for sale to Loans and advances (c)
Carrying amount of assets reclassified in 2008	-	-	17,855
Carrying amount of reclassified assets, as of December 31, 2017	-	-	3,735
Fair value of reclassified assets as of December 31, 2017	-	-	2,974
AMOUNT NOT RECOGNIZED THROUGH PROFIT AND LOSS (a) AND (b) DUE TO RECLASSIFICATION	-	-	-
AMOUNT NOT RECOGNIZED THROUGH ASSETS AVAILABLE FOR SALE (c) DUE TO RECLASSIFICATION	-	-	(761)
Premium/discount amortization through profit and loss in 2017	-	-	-
Premium/discount amortization through AFS reserve in 2017 ⁽¹⁾	-	-	3

(1) The balance remaining for amortization at the end of 2017 totaled EUR -78 million (see note 4.4)

3. NOTES TO THE LIABILITIES (EUR millions)

3.1 - DUE TO BANKS

3.1.1. Analysis by nature

	12/31/2015	12/31/2016	12/31/2017
Term borrowing - parent company	5,511	5,220	4,821
Interest accrued not yet due	9	5	0
Sight accounts	-	-	-
TOTAL	5,520	5,225	4,821

At the end of December 2017, the funding borrowed from SFIL within the framework of the financing agreement was comprised of different loans with maturities that could initially run from one day to ten years with an Euribor or Eonia index.

3.1.2. Analysis by term to maturity

See note 7.4

3.2 - DEBT SECURITIES

3.2.1. Analysis by nature

	12/31/2015	12/31/2016	12/31/2017
Obligations foncières	49,643	48,289	45,157
Registered covered bonds	7,499	7,821	7,741
TOTAL	57,142	56,110	52,898

3.2.2. Analysis by term to maturity

See note 7.4

3.3 - TAX LIABILITIES

	12/31/2015	12/31/2016	12/31/2017
Current income tax	0	0	0
Other taxes	1	0	0
Current tax liabilities	1	0	0
Deferred tax liabilities (see note 4.2)	-	-	-
TOTAL TAX LIABILITIES	1	0	0

3.4 - ACCRUALS AND OTHER LIABILITIES

	12/31/2015	12/31/2016	12/31/2017
Cash collateral received	1,397	1,263	687
Other accrued charges	15	16	24
Deferred income	-	-	-
Contribution to support funds ⁽¹⁾	162	136	110
Other accounts payable and other liabilities	10	9	2
TOTAL	1,584	1,424	823

(1) This item represents the commitments taken by Caisse Française de Financement Local to contribute to the pluri-annual support funds:

- in 2013, for local governments in the amount of EUR 10 million for 15 years (EUR 150 million);

- in 2014 and 2015 for public hospitals in the amount of respectively EUR 18 million (EUR 6 million for three years) and EUR 20 million (EUR 10 million for two years).

3.5 - PROVISIONS

For the record, in 2015, French tax authorities investigated the income declared and the tax paid for 2012 and 2013. Following the tax assessment, the tax authorities expressed their disagreement with the tax treatment of the following two points: the taxation in Ireland of the income from the Dublin branch of Dexia Municipal Agency, which was closed in 2013, and the deductibility of provisions for non-performing loans. In order to safeguard its rights to the disputed adjustment, in 2017 the tax authority initiated a verification procedure relating to the consequences of its previous assessment of taxable income for the 2014 to 2016 fiscal years. The two points of disagreement resulting from the 2015 assessment still held following this tax audit. There were no other new developments.

In 2016 and 2017, Caisse Française de Financement Local introduced the right of appeal stipulated by regulations and maintained its position. Neither the discussions that took place with the tax authorities nor the new tax audit called into question the assumptions used to calculate the amount provisioned in the accounts. The provisions recorded in 2015 were however adjusted for due interest.

4. OTHER NOTES ON THE BALANCE SHEET (EUR millions)

4.1 - DERIVATIVES

4.1.1. Analysis by nature

	12/31/2015		12/31/2016		12/31/2017	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
Derivatives at fair value through profit or loss ⁽¹⁾	2	2	0	4	-	4
Derivatives designated as fair value hedges	4,643	8,117	4,517	6,419	3,268	5,288
Derivatives designated as cash flow hedges	6	162	5	140	2	56
Derivatives designated as portfolio hedges	2,397	3,811	1,918	3,283	1,360	2,587
Hedging derivatives	7,046	12,090	6,440	9,842	4,630	7,931
CVA / DVA Impact	(3)	(77)	(3)	(45)	(1)	(1)
TOTAL FAIR VALUE OF DERIVATIVES	7,045	12,015	6,437	9,801	4,629	7,934

(1) Caisse Française de Financement Local is only authorized to conduct derivative transactions for purposes of hedging. Some hedging derivatives, which do not comply with all the conditions required by IFRS, are reported in the item Derivatives at fair value through profit and loss.

4.1.2. Detail of derivatives designated as fair value hedges

	12/31/2015			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Foreign exchange derivatives	7,052	6,952	482	372
Interest rate derivatives	57,560	57,541	4,161	7,745
TOTAL	64,612	64,493	4,643	8,117

	12/31/2016			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Foreign exchange derivatives	5,979	5,670	590	304
Interest rate derivatives	55,827	55,801	3,927	6,115
TOTAL	61,806	61,471	4,517	6,419

	12/31/2017			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Foreign exchange derivatives	6,484	6,601	174	323
Interest rate derivatives	67,666	67,661	3,094	4,965
TOTAL	74,150	74,262	3,268	5,288

4.1.3. Detail of derivatives designated as cash flow hedges

	12/31/2015			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Foreign exchange derivatives	954	1,071	6	162
Interest rate derivatives	-	-	-	-
TOTAL	954	1,071	6	162

	12/31/2016			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Foreign exchange derivatives	825	923	5	140
Interest rate derivatives	-	-	-	-
TOTAL	825	923	5	140

	12/31/2017			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Foreign exchange derivatives	499	521	2	56
Interest rate derivatives	-	-	-	-
TOTAL	499	521	2	56

	12/31/2015	12/31/2016	12/31/2017
Amount removed from cash flow hedge reserve and included in the carrying amount of a non-financial instrument (hedging of cash flows of a highly probable transaction)	-	-	-

4.1.4. Detail of derivatives designated as portfolio hedges

	12/31/2015			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Interest rate derivatives	90,293	90,288	2,397	3,811
TOTAL	90,293	90,288	2,397	3,811
	12/31/2016			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Interest rate derivatives	78,519	78,514	1,918	3,283
TOTAL	78,519	78,514	1,918	3,283
	12/31/2017			
	Notional amount		Assets	Liabilities
	To receive	To deliver		
Interest rate derivatives	55,848	55,813	1,360	2,587
TOTAL	55,848	55,813	1,360	2,587

4.2 - DEFERRED TAXES

Deferred tax assets and liabilities are netted out when they concern the same tax entity.

4.2.1. Analysis by nature

	12/31/2015	12/31/2016	12/31/2017
Deferred tax assets before impairment	108	109	69
Impairment on deferred tax assets	-	-	-
Deferred tax assets	108	109	69
Deferred tax liabilities	-	-	-
TOTAL	108	109	69

4.2.2. Movements

	12/31/2015	12/31/2016	12/31/2017
As of January 1	99	108	109
Charge/credit recognized in the income statement	27	7	(25)
Effect of change in tax rates - impact on the income statement ⁽¹⁾	-	(14)	(2)
Movements directly recognized in equity	(18)	8	(13)
Effect of change in tax rates - impact on equity	-	-	-
Translation adjustment	-	-	-
Other movements	-	-	-
As of end of period	108	109	69

(1) In 2017, Caisse Française de Financement Local has taken note of the reduction in corporate income tax to 25% as of 2022. To this end, it reduced its deferred tax assets and recorded a non-recurring expense of EUR - 2 million in its accounts. For the record, in 2016, Caisse Française de Financement Local also took into account legislative measures reducing the tax rate to 28% from 2020, and recorded a non-recurring expense of EUR -14 million.

4.2.3. Deferred taxes from assets on the balance sheet

	12/31/2015	12/31/2016	12/31/2017
Loans and loan loss provisions	80	359	725
Securities	46	58	61
Derivatives	167	(157)	(198)
Accruals and other assets	14	13	14
TOTAL	307	273	602

4.2.4. Deferred taxes from liabilities on the balance sheet

	12/31/2015	12/31/2016	12/31/2017
Borrowings, deposits and issues of debt securities	(199)	(164)	(533)
Derivatives	-	-	-
Provisions	-	-	-
Accruals and other liabilities	-	-	-
TOTAL	(199)	(164)	(533)

4.3 - TRANSACTIONS WITH RELATED-PARTIES

Analysis by nature

	Parent company ⁽¹⁾			Other related parties ⁽²⁾		
	12/31/2015	12/31/2016	12/31/2017	12/31/2015	12/31/2016	12/31/2017
ASSETS						
Loans and advances	2,341	-	578	-	-	-
Bonds	-	-	-	-	-	9
LIABILITIES						
Due to banks - sight accounts	-	-	-	-	-	-
Due to banks - term loans	5,520	5,225	4,821	-	-	-
INCOME STATEMENT						
Interest income on loans and advances	11	6	1	(9)	(12)	(11)
Interest income on bonds	-	-	-	-	(0)	(0)
Interest expense on borrowings	(37)	(25)	(11)	-	-	-
Fees and commissions	(19)	(3)	(11)	-	(0)	(0)
OFF-BALANCE SHEET						
Foreign exchange derivatives	4,399	3,508	1,490	-	-	-
Interest rate derivatives	17,487	13,847	14,018	-	-	-
Commitments and guarantees received	2,391	50	50	140	52	-
Commitments and guarantees given	600	3,722	3,028	-	-	-

(1) This item includes transactions with SFIL, the parent company of Caisse Française de Financement Local.

(2) This items may includes transactions with Caisse des dépôts et consignations and La Banque Postale, shareholders of SFIL.

4.4 - UNREALIZED OR DEFERRED GAINS AND LOSSES, BREAKDOWN BY COUNTRY

	12/31/2015	12/31/2016	12/31/2017
Unrealized gains and losses on available for sale securities	(48)	(78)	(49)
Belgium	-	-	0
Canada	0	0	-
Spain	-	(0)	1
United States	(4)	(10)	0
France	(2)	(4)	(2)
Italy	(42)	(64)	(48)
Norway	-	-	(0)
Sweden	-	-	(0)
Unrealized gains and losses on loans and receivable securities	(85)	(81)	(78)
Spain	(1)	(1)	(1)
France	3	3	2
Italy	(87)	(83)	(79)
Unrealized gains and losses on derivatives designated as cash-flow hedges	(39)	(35)	(30)
TOTAL	(172)	(194)	(157)
Deferred taxes on gains and losses, available for sale securities	17	27	17
Deferred taxes on gains and losses, loans and receivable securities	29	28	27
Deferred taxes on gains and losses, derivatives designated as cash-flow hedges	13	12	10
TOTAL	(113)	(127)	(103)

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4.5 BREAKDOWN OF GOVERNMENT BONDS IN A SELECTION OF EUROPEAN COUNTRIES

The credit risk exposure reported represents the accounting net carrying amount of exposures, being the notional amounts after deduction of specific impairment and AFS reserves, and taking into account accrued interest.

	12/31/2016					Total
	Spain	Ireland	Italy	Portugal	Greece	
Financial assets available for sale	201	-	458	-	-	659
Financial assets held for trading	-	-	-	-	-	-
Held to maturity investments	-	-	-	-	-	-
Loans and advances	-	-	113	-	-	113
TOTAL	201	-	571	-	-	772
UNREALIZED GAINS AND LOSSES ON AVAILABLE FOR SALE SECURITIES	(0)	-	(64)	-	-	(64)
UNREALIZED GAINS AND LOSSES ON LOANS AND RECEIVABLE SECURITIES	-	-	-	-	-	-

	12/31/2017					Total
	Spain	Ireland	Italy	Portugal	Greece	
Financial assets available for sale	203	-	451	-	-	654
Financial assets held for trading	-	-	-	-	-	-
Held to maturity investments	-	-	-	-	-	-
Loans and advances	-	-	112	-	-	112
TOTAL	203	-	563	-	-	766
UNREALIZED GAINS AND LOSSES ON AVAILABLE FOR SALE SECURITIES	1	-	(48)	-	-	(47)
UNREALIZED GAINS AND LOSSES ON LOANS AND RECEIVABLE SECURITIES	-	-	-	-	-	-

5. NOTES TO THE INCOME STATEMENT (EUR millions)

5.1 - INTEREST INCOME - INTEREST EXPENSE

	2016	2017
INTEREST INCOME	3,256	2,645
Central banks	-	-
Loans and advances due from banks	23	9
Loans and advances to customers	1,428	1,330
Financial assets available for sale	38	36
Financial assets held to maturity	-	-
Derivatives used for hedging	1,767	1,271
Impaired assets	-	-
Other	0	(1)
INTEREST EXPENSE	(3,106)	(2,460)
Accounts with central banks	(14)	(13)
Due to banks	(19)	(7)
Customer borrowings and deposits	-	-
Debt securities	(1,583)	(1,299)
Subordinated debt	-	-
Derivatives used for hedging	(1,489)	(1,141)
Other	(1)	(0)
INTEREST MARGIN	150	185

5.2 - FEES AND COMMISSIONS

	2016			2017		
	Income	Expense	Net	Income	Expense	Net
Lending activity	0	-	0	0	-	0
Purchase and sale of securities	-	(1)	(1)	-	(1)	(1)
Services on securities other than custodian services	-	(3)	(3)	-	(3)	(3)
Commissions on financial instruments	-	(0)	(0)	3	-	3
Rebilling by parent company	-	(3)	(3)	-	(11)	(11)
TOTAL	0	(7)	(7)	3	(15)	(12)

5.3 - NET RESULT OF FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS

All interest received and paid on assets, liabilities and derivatives is recorded in net interest income, as required by IFRS. Thus, net gains (losses) on trading transactions and net gains (losses) on hedging transactions include only the change in the clean value of derivatives and the revaluation of assets and liabilities qualified as hedges and the revaluation of the portfolio held for trading.

	2016	2017
Net trading income	(1)	4
Net result of hedge accounting	(36)	(37)
Net result of foreign exchange transactions	(1)	0
TOTAL	(38)	(33)

Analysis of net result of hedge accounting

	2016	2017
Fair value hedges	(3)	5
Fair value changes in the hedged item attributable to the hedged risk	508	3
Fair value changes in the hedging derivatives	(511)	2
Cash flow hedges	-	-
Fair value changes in the hedging derivatives - ineffective portion	-	-
Discontinuation of cash flow hedge accounting (Cash flows no longer expected to occur)	-	-
Portfolio hedge	(1)	-
Fair value changes in the hedged item	12	(223)
Fair value changes in the hedging derivatives	(13)	223
CVA / DVA Impact⁽¹⁾	(32)	(42)
TOTAL	(36)	(37)

(1) As of December 31, 2017, the application of IFRS 13 shows a net impact of EUR -42 million comprised of EUR -44 million for DVA and EUR +2 million for CVA.

5.4 - NET RESULT OF FINANCIAL ASSETS AVAILABLE FOR SALE

	2016	2017
Net result of disposals of loans and securities available for sale	(0)	0
Net result of disposals of debt securities	(1)	(1)
Net result of the sale or cancellation of loans and advances	15	17
TOTAL	14	16

5.5 - OPERATING EXPENSE

	2016	2017
Payroll costs	-	-
Other general and administrative expense ⁽¹⁾	(91)	(98)
Taxes	(7)	(7)
TOTAL	(98)	(105)

(1) Of which EUR 95 million to the benefit of SFIL as of December 31, 2017.

Caisse Française de Financement Local has no salaried employees in accordance with article L.513-15 of the Monetary and Financial Code. The general management of the operations of Caisse Française de Financement Local has been entrusted by an agreement to its parent company, SFIL, a credit institution.

Specific individual agreements have been established with entities that have transferred assets to the société de crédit foncier, and continue to ensure management for their national clientèle. These assets are managed in a run-off mode. At the end of December 2017, there were agreements with the following entities : Kommunalkredit Austria (Austria), Belfius Banque et Assurances (Belgium), and Dexia Crediop (Italy). These agreements already existed in previous years.

Management of registered covered bonds (RCB) issued since 2015 is entrusted to Landesbank Baden-Württemberg (LBBW). Dexia Kommunalbank Deutschland continues to manage registered covered bonds issued prior to 2015.

5.6 - COST OF RISK

	2016		
	Collective impairment	Specific impairment and losses	Total
Credit (loans, commitments and securities held to maturity)	18	0	18
Fixed income securities available for sale	-	-	-
TOTAL	18	0	18

	2017		
	Collective impairment	Specific impairment and losses	Total
Credit (loans, commitments and securities held to maturity)	16	6	22
Fixed income securities available for sale	-	-	-
TOTAL	16	6	22

Detail of collective and specific impairments

Collective impairment	2016			2017		
	Allocations	Reversals	Total	Allocations	Reversals	Total
Loans and borrowings	(2)	20	18	(1)	17	16
Off-balance sheet commitments	-	-	-	-	-	-
TOTAL	(2)	20	18	(1)	17	16

Specific Impairment	2016				
	Allocations	Reversals	Losses	Recoveries	Total
Loans and advances due from banks	-	-	-	-	-
Loans and advances to customers	(2)	2	(0)	-	0
Financial assets held to maturity	-	-	-	-	-
Off-balance sheet commitments	-	-	-	-	-
Total credit	(2)	2	(0)	-	0
Fixed income securities	-	-	-	-	-
TOTAL	(2)	2	(0)	-	0

Specific Impairment	2017				
	Allocations	Reversals	Losses	Recoveries	Total
Loans and advances due from banks	-	-	-	-	-
Loans and advances to customers	(0)	6	-	-	6
Financial assets held to maturity	-	-	-	-	-
Off-balance sheet commitments	-	-	-	-	-
Total credit	(0)	6	-	-	6
Fixed income securities	-	-	-	-	-
TOTAL	(0)	6	-	-	6

5.7 - CORPORATE INCOME TAX

5.7.1. Breakdown of tax expense

	2016	2017
Current taxes	(22)	(2)
Deferred taxes	(7)	(27)
Tax on prior years' income	-	-
Deferred taxes on prior years	-	-
Provisions for tax litigation	-	(3)
TOTAL	(29)	(32)

5.7.2. Effective tax expense

The difference between the actual corporate income tax rate and the French tax rate can be analysed as follow:

	2016	2017
INCOME BEFORE INCOME TAXES	39	73
TAX BASE	39	73
Applicable tax rate at end of the period	34.43%	34.43%
THEORETICAL CORPORATE INCOME TAX AT THE STANDARD RATE	(14)	(26)
Tax effect of non-deductible expenses	(1)	(1)
Tax effect of non-taxable income	-	-
Impact of items taxed at a reduced rate	-	-
Other additional taxes or tax savings	0	(0)
Liability method	-	-
Provisions for tax litigation	-	(3)
Change in corporate income tax rate applicable to future fiscal years ⁽¹⁾	(14)	(2)
CORPORATE INCOME TAX RECORDED IN THE INCOME STATEMENT	(29)	(32)

(1) In 2017, Caisse Française de Financement Local has taken note of the reduction in corporate income tax to 25% as of 2022. To this end, it reduced its deferred tax assets and recorded a non-recurring expense of EUR -2 million in its accounts. For the record, in 2016, Caisse Française de Financement Local also took into account legislative measures reducing the tax rate to 28% from 2020, and recorded a non-recurring expense of EUR -14 million.

5.7.3. Tax consolidation

Since January 1, 2014, Caisse Française de Financement Local has been a member of the SFIL tax group.

6. NOTE ON OFF-BALANCE SHEET ITEMS (EUR millions)

6.1 - REGULAR WAY TRADE

	12/31/2015	12/31/2016	12/31/2017
Assets to be delivered	-	-	-
Liabilities to be received	-	-	-

6.2 - GUARANTEES

	12/31/2015	12/31/2016	12/31/2017
Guarantees received from credit institutions ⁽¹⁾	2,525	84	22
Enhanced guarantees ⁽²⁾	-	3,722	3,247
Guarantees received from customers ⁽³⁾	5,867	2,863	2,549

(1) Readers are reminded that at the end of 2015, Caisse Française de Financement Local received some securities in guarantee in exchange for refinancing granted to its parent company SFIL in the amount of EUR 2,3 billion. This refinancing was fully repaid in 2016.

(2) Irrevocable and unconditional 100% guarantee issued by the French State to the benefit of Caisse Française de Financement Local for the refinancing of large export credits.

(3) Guarantees received from customers are generally granted by local governments.

6.3 - FINANCING COMMITMENTS

	12/31/2015	12/31/2016	12/31/2017
Loan commitments granted to credit institutions ⁽¹⁾	600	3,722	3,028
Loan commitments granted to customers ⁽²⁾	293	125	90
Loan commitments received from credit institutions ⁽³⁾	50	50	50
Loan commitments received from customers	-	-	-

(1) Within the framework of the large export credit refinancing business, the balance corresponded to a commitment of Caisse Française de Financement Local to finance its parent company (SFIL).

(2) The financing commitments on loans corresponded to contracts issued but not paid out at the end of year.

(3) This item concerned the amount of the overdraft authorized on the current account with SFIL, which totaled EUR 50 million. Readers are reminded that SFIL is committed to providing unlimited funding to Caisse Française de Financement Local through financing agreements between the two companies.

6.4 - OTHER COMMITMENTS

	12/31/2015	12/31/2016	12/31/2017
Commitments given ⁽¹⁾	-	-	3
Commitments received ⁽²⁾	238	232	226

(1) It means the irrevocable payment commitment to the Fonds de garantie des dépôts et de résolution.

(2) They mainly concern a loan granted to a credit institution and guaranteed by a public sector entity.

7. NOTES ON RISK EXPOSURE (EUR millions)

7.1 - FAIR VALUE

This note presents the fair value adjustments that are not accounted for in income or in equity, because they correspond to assets or liabilities valued at amortized cost in the IFRS financial statements.

These fair value adjustments take into account the characteristics of the assets and liabilities concerned (maturity, interest rate risk hedging, amortization profile, and for assets, the rating); they are also influenced by current market conditions for these very operations or operations to which they can be assimilated, in particular in terms of price and spread. The breakdown of assets and liabilities in function of the method used to determine their fair value is presented in note 7.1.3. below; in fact, the great majority of the assets are valued according to a technique that accounts for the fact that significant parameters are not observable for the assets, since exposure mainly concerns loans, a commitment format that is not listed in liquid markets. To value liabilities, certain observable parameters are taken into account.

These fair values provide interesting information, but it would not be relevant to draw conclusions about the value of the Company or the results it will achieve in the future. Indeed, assets and liabilities present good congruence in interest rates and maturities and are meant to be held on the balance sheet to maturity, because of the specialized business the Company does.

7.1.1. Composition of the fair value of assets

	12/31/2016		
	Book value	Fair value	Unrecognized fair value adjustment
Central banks	3,684	3,684	-
Loans and advances due from banks	381	375	(6)
Loans and advances to customers	59,679	58,277	(1,402)
Financial assets available for sale	1,736	1,736	-
Derivatives	6,437	6,437	-
TOTAL	71,917	70,509	(1,408)

	12/31/2017		
	Book value	Fair value	Unrecognized fair value adjustment
Central banks	1,706	1,706	-
Loans and advances due from banks	867	879	12
Loans and advances to customers	56,892	54,015	(2,877)
Financial assets available for sale	2,048	2,048	-
Derivatives	4,629	4,629	-
TOTAL	66,142	63,277	(2,865)

7.1.2. Composition of the fair value of liabilities, excluding equity

	12/31/2016		
	Book value	Fair value	Unrecognized fair value adjustment
Due to banks	5,225	5,260	35
Debt securities	56,110	57,231	1,121
Derivatives	9,801	9,801	-
TOTAL	71,136	72,292	1,156

	12/31/2017		
	Book value	Fair value	Unrecognized fair value adjustment
Due to banks	4,821	4,834	13
Debt securities	52,898	54,205	1,307
Derivatives	7,934	7,934	-
TOTAL	65,653	66,973	1,320

7.1.3. Methods used to determine the fair value of financial instruments

The fair value of a financial instrument is determined on the basis of prices that can be observed in the market for the instrument itself or for a comparable instrument, or with the help of a technical evaluation utilizing observable market data. A hierarchy of the methods used to establish fair value has been drawn up. It is composed of the following three levels.

- Level 1 corresponds to the instruments considered to be liquid, i.e. that their valuation is based on the price observed in a liquid market, for which Caisse Française de Financement Local assured itself of the existence of a large number of contributors. Level 1 securities include in particular certain government bonds.
- Level 2 uses another method to determine the value of instruments for which Caisse Française de Financement Local can not observe market prices, but observes such for similar instruments by the same issuer or guarantor listed in the market. In this case, observable prices and other data observable in the market are used and an adjustment is made to account for the degree of the security's lack of liquidity.
- In level 3, when there is no active market or observable market data, the fair value of instruments is determined by using a valuation spread developed from an internal model. Derivatives are valued using these internal models.

The measurement of derivatives is based on an analysis combining the observability of the market data used in the assessment and the robustness of the valuation models measured in terms of efficiency to provide a valuation in market consensus. The result of this application is that the derivatives used by Caisse Française de Financement Local in hedging its activities are primarily of level 2.

For the derivatives in level 3, this classification mainly involves hybrid, structured products (interest rate – foreign exchange), spread (correlation) products and options on interest rates. This classification is mainly due to the fact that these products present complex payoffs which require an advanced statistical model with variable parameters which are sometimes unable to be seen in the market.

Fair value of financial assets	12/31/2016			
	Level 1	Level 2	Level 3	Total
Central banks	3,684	-	-	3,684
Loans and advances due from banks	4	-	371	375
Loans and advances to customers	1,475	2,366	54,436	58,277
Subtotal of assets at amortized costs	5,163	2,366	54,807	62,336
Financial assets available for sale	924	812	-	1,736
Derivatives	-	5,837	600	6,437
Subtotal of assets at fair value	924	6,649	600	8,173
TOTAL	6,087	9,015	55,407	70,509

Fair value of financial assets	12/31/2017			
	Level 1	Level 2	Level 3	Total
Central banks	1,706	-	-	1,706
Loans and advances due from banks	10	579	290	879
Loans and advances to customers	488	2,868	50,659	54,015
Subtotal of assets at amortized costs	2,204	3,447	50,949	56,600
Financial assets available for sale	1,561	487	-	2,048
Derivatives	-	4,067	562	4,629
Subtotal of assets at fair value	1,561	4,554	562	6,677
TOTAL	3,765	8,001	51,511	63,277

Fair value of financial liabilities	12/31/2016			
	Level 1	Level 2	Level 3	Total
Due to banks	-	5,260	-	5,260
Debt securities	-	57,231	-	57,231
Subtotal of liabilities at amortized costs	-	62,491	-	62,491
Derivatives	-	8,547	1,254	9,801
Subtotal of assets at fair value	-	8,547	1,254	9,801
TOTAL	-	71,038	1,254	72,292

Fair value of financial liabilities	12/31/2017			
	Level 1	Level 2	Level 3	Total
Due to banks	-	4,834	-	4,834
Debt securities	-	54,205	-	54,205
Subtotal of liabilities at amortized costs	-	59,039	-	59,039
Derivatives	-	7,092	842	7,934
Subtotal of assets at fair value	-	7,092	842	7,934
TOTAL	-	66,131	842	66,973

Sensitivity of the market value of level 3 financial instruments to changes in reasonably possible hypotheses

The following table gives a synthetic view of financial instruments in level 3 for which changes in hypotheses concerning one or more non observable parameter would cause a significant change in market value. These amounts illustrate the interval of uncertainty inherent in the recourse to judgment in estimating parameters of level 3 or in the choice of valuation techniques and models. They reflect the uncertainty of valuation which is effective at the date of valuation. Although this uncertainty essentially results from the sensitivity of the portfolio at the date of valuation, it does not make it possible to foresee or to deduct future variations in the market value any more than they represent the effect of extreme market conditions on the value of the portfolio. To estimate sensitivity, Caisse Française de Financement Local either values financial instruments using reasonably possible parameters or applies hypotheses based on its policy of additional valuation adjustments.

	12/31/2016	12/31/2017
Uncertainty inherent in level 3 market parameters	20	5
Uncertainty inherent in level 3 derivatives valuation models	32	36
SENSITIVITY OF THE MARKET VALUE OF LEVEL 3 FINANCIAL INSTRUMENTS	52	41

7.1.4. Transfer between levels 1 and 2

	12/31/2016	12/31/2017
Level 1 to level 2	-	-
TOTAL	-	-

7.1.5. Level 3: flow analysis

Fair value of financial assets	Financial assets available for sale	Derivatives	TOTAL FINANCIAL ASSETS	Derivatives	TOTAL FINANCIAL LIABILITIES
12/31/2016	-	600	600	1,254	1,254
Total gains and losses through profit and loss	-	1	1	(49)	(49)
Total unrealized or deferred gains and losses	-	(22)	(22)	152	152
Total OCI unrealized or deferred gains and losses	-	-	-	-	-
Purchase	-	3	3	2	2
Sale	-	-	-	-	-
Direct origination	-	-	-	-	-
Settlement	-	2	2	-	-
Transfer in activities destined to be sold	-	-	-	-	-
Transfer to level 3	-	-	-	83	83
Transfer out of level 3	-	(22)	(22)	(600)	(600)
Other variations	-	-	-	-	-
12/31/2017	-	562	562	842	842

7.2 - OFFSETTING FINANCIAL ASSETS AND LIABILITIES

7.2.1. Financial assets subject to off-setting, enforceable master netting arrangements and similar agreements

	12/31/2016					
	Gross amounts before off-setting	Gross amounts off-set according to IAS 32	Net amounts presented on the balance sheet	Other amounts in the scope of application but not off-set		Net Amounts according to IFRS 7 & 13
				Effect of master netting arrangements	Financial Instruments received as collateral	
Derivatives (including hedging instruments)	6,437	-	6,437	(5,101)	(1,104)	232
Loans and advances due from banks	381	-	381	-	-	381
Loans and advances to customers	59,679	-	59,679	-	-	59,679
TOTAL	66,497	-	66,497	(5,101)	(1,104)	60,292

	12/31/2017					Net amounts according to IFRS 7 & 13
	Gross amounts before off-setting	Gross amounts off-set according to IAS 32	Net Amounts presented in the balance sheet	Other amounts in the scope of application but not off-set		
				Effect of master netting arrangements	Financial instruments received as collateral	
Derivatives (including hedging instruments)	4,629	-	4,629	(3,964)	(605)	60
Loans and advances due from banks	867	-	867	-	-	867
Loans and advances to customers	56,892	-	56,892	-	-	56,892
TOTAL	62,388	-	62,388	(3,964)	(605)	57,819

7.2.2. Financial liabilities subject to offsetting, enforceable master netting arrangements and similar agreements

	12/31/2016					Net amounts according to IFRS 7 & 13
	Gross amounts before off-setting	Gross amounts off-set according to IAS 32	Net amounts presented on the balance sheet	Other amounts in the scope of application but not off-set		
				Effect of master netting arrangements	Financial instruments received as collateral	
Derivatives (including hedging instruments)	9,801	-	9,801	(5,101)	-	4,700
Due to banks	5,225	-	5,225	-	-	5,225
Customer borrowings and deposits	-	-	-	-	-	-
TOTAL	15,026	-	15,026	(5,101)	-	9,925

	12/31/2017					Net amounts according to IFRS 7 & 13
	Gross amounts before off-setting	Gross amounts off-set according to IAS 32	Net amounts presented on the balance sheet	Other amounts in the scope of application but not off-set		
				Effect of master netting arrangements	Financial instruments received as collateral	
Derivatives (including hedging instruments)	7,934	-	7,934	(3,964)	-	3,970
Due to banks	4,821	-	4,821	-	-	4,821
Customer borrowings and deposits	-	-	-	-	-	-
TOTAL	12.755	-	12.755	(3.964)	-	8.791

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7.3 - EXPOSURE TO CREDIT RISK

Exposure to credit risks, as presented to management, includes the following:

- for assets other than derivatives: the amount on the balance sheet (i.e. after deduction of specific provisions);
- for derivatives: the market value on the balance sheet (i.e. after deduction of cash collateral and CVA provisions);
- for off-balance sheet commitments: the amount intact of financing commitment drawdowns, is stated in the notes to the financial statements.

Exposure to credit risk is broken down by region and by counterparty, taking into account the guarantees received. This signifies that when the credit risk is guaranteed by a third party whose weighted risk (in the sense of Basel regulations) is less than that of the direct borrower, exposure is included in the guarantor's region and business sector.

7.3.1. Breakdown of exposure to credit risks

Analysis of exposure by geographic region

	12/31/2016	12/31/2017
France	61,610	57,703
Italy	6,687	6,156
Germany	611	341
Spain	441	378
United Kingdom	283	199
Belgium	176	159
Other European Union countries	273	359
Norway	-	79
Switzerland	1,685	1,339
United States and Canada	700	513
Japan	40	39
TOTAL EXPOSURE	72,506	67,265

Analysis of exposure by category of counterparty

	12/31/2016	12/31/2017
States	10,020	7,430
Local public sector	61,518	58,753
Other assets guaranteed by public sector entities	14	12
Financial institutions	954	1,070
TOTAL EXPOSURE	72,506	67,265

Exposure on financial institutions is primarily comprised of counterparties in hedging derivatives and replacement assets. As of December 31, 2017, Caisse Française de Financement Local had no asset-backed securities.

Analysis of exposure by category of instrument

	12/31/2016	12/31/2017
Debt securities	1,746	2,066
Loans and advances	66,883	62,047
Financing commitments on loans	3,847	3,118
Derivatives	30	34
TOTAL EXPOSURE	72,506	67,265

7.3.2. Evaluation of asset credit quality

Caisse Française de Financement Local decided to use the advanced method recommended by the regulators in relation to the Basel III reforms on the capital adequacy ratio and capital requirements. Caisse Française de Financement Local has developed internal rating models covering the main client segments. These models were validated by the banking supervisors who authorized the Group to use these advanced internal models for the calculation and reporting of equity requirements for credit risk as of January 1, 2008. This enables Caisse Française de Financement Local to present on December 31, 2017, an analysis of its exposures, broken down by risk weighting, as used to calculate equity requirements. Credit weighting is mainly calculated on the basis of the probability of default of the counterparty and of the loss incurred in the event of default.

This analysis confirms the excellent quality of the assets in Caisse Française de Financement Local's portfolio. More than 81% of the portfolio has a weighting of less than 5% and 96% of the portfolio has a weighting that is less than or equal to 20%.

	Risk weighting (Basel III)				Total
	From 0 to 5%	From 5% to 20%	From 20% to 50%	More than 50%	
Debt securities	488	604	346	628	2,066
Loans and advances	51,083	9,118	269	1,578	62,048
Financing commitments on loans	3,117	-	-	-	3,117
Derivatives	3	16	8	7	34
TOTAL EXPOSURE	54,691	9,738	623	2,213	67,265
SHARE	81.3%	14.5%	0.9%	3.3%	100.0%

Certain exposures do not yet benefit from an internal rating system validated by banking supervisors; in this case, their weighting is the one in the standard method, which is, for example, 20% for French local governments.

7.4 - LIQUIDITY RISK: ANALYSIS BY TERM TO MATURITY

7.4.1. Breakdown of assets

	12/31/2017						
	Sight	Less than 3 months	3 months to 1 year	1 to 5 years	More than 5 years	No fixed maturity	Total broken down
Central banks	1,706	-	-	-	-	-	1,706
Derivatives	-	-	-	-	-	-	-
Financial assets available for sale	-	276	349	792	429	-	1,846
Loans and advances due from banks	10	550	198	23	84	-	865
Loans and advances to customers	5	7,077	8,369	11,929	25,925	-	53,305
Fair value revaluation of portfolio hedge	-	-	-	-	-	-	-
Financial assets held to maturity	-	-	-	-	-	-	-
Tax assets	-	-	0	-	-	69	69
Accruals and other assets	-	26	14	-	8	-	48
TOTAL	1,721	7,929	8,930	12,744	26,446	69	57,839

	12/31/2017				
	Total broken down	Accrued interest	Fair value adjustment	Impairment	Total
Central banks	1,706	-	-	-	1,706
Derivatives	-	637	3,992	-	4,629
Financial assets available for sale	1,846	14	188	-	2,048
Loans and advances due from banks	865	1	1	-	867
Loans and advances to customers	53,305	593	3,047	(53)	56,892
Fair value revaluation of portfolio hedge	-	-	2,518	-	2,518
Financial assets held to maturity	-	-	-	-	-
Tax assets	69	-	-	-	69
Accruals and other assets	48	-	-	-	48
TOTAL	57,839	1,245	9,746	(53)	68,777

7.4.2. Breakdown of liabilities, excluding equity

12/31/2017							
	Sight	Less than 3 months	3 months to 1 year	1 to 5 years	More than 5 years	No fixed maturity	Total broken down
Central banks	-	-	-	-	-	-	-
Derivatives	-	-	-	-	-	-	-
Due to banks	-	200	587	2,465	1,569	-	4,821
Customer borrowings and deposits	-	-	-	-	-	-	-
Debt securities	-	1,722	2,002	17,662	28,201	-	49,587
Fair value revaluation of portfolio hedge	-	-	-	-	-	-	-
Tax liabilities	-	-	0	-	-	-	0
Accruals and other liabilities	-	723	-	40	60	-	823
Provisions	-	-	-	41	-	-	41
Subordinated debt	-	-	-	-	-	-	-
TOTAL	-	2,645	2,589	20,207	29,830	-	55,272

12/31/2017				
	Total broken down	Accrued interest	Fair value adjustment	Total
Central banks	-	-	-	-
Derivatives	-	548	7,386	7,934
Due to banks	4,821	0	-	4,821
Customer borrowings and deposits	-	-	-	-
Debt securities	49,587	741	2,570	52,898
Fair value revaluation of portfolio hedge	-	-	883	883
Tax liabilities	0	-	-	0
Accruals and other liabilities	823	(0)	-	823
Provisions	41	-	-	41
Subordinated debt	-	-	-	-
TOTAL	55,272	1,289	10,839	67,400

7.4.3. Net liquidity gap

12/31/2017								
	Sight	Less than 3 months	3 months to 1 year	1 to 5 years	More than 5 years	No fixed maturity	Total not broken down	Total
AMOUNT	1,721	5,284	6,341	(7,464)	(3,384)	69	(1,190)	1,377

This table presents the balance sheet at the closing date; it does not take into account the management decisions that will make it possible to manage differences in maturity or the future production of assets and liabilities. Caisse Française de Financement Local's liquidity is provided by its refinancing agreement with SFIL. In addition, the Company may obtain funding from the Banque de France, by giving certain of these assets in guarantee. In addition to access to the central bank in its own name, Caisse Française de Financement Local can also mobilize certain of these eligible assets by using interbank financing in the form of repurchase agreements. If necessary, these transactions would easily cover its cash flow requirements.

7.5 - RISK ON RESETTING OF INTEREST RATES: ANALYSIS BY TIME BUCKET UNTIL NEXT INTEREST RATE RESET DATE

7.5.1. Breakdown of assets

	12/31/2017						
	Sight	Less than 3 months	3 months to 1 year	1 to 5 years	More than 5 years	No fixed maturity	Total broken down
Central banks	1,706	-	-	-	-	-	1,706
Derivatives	-	-	-	-	-	-	-
Financial assets available for sale	-	276	349	792	429	-	1,846
Loans and advances due from banks	10	550	198	23	84	-	865
Loans and advances to customers	5	7,077	8,369	11,929	25,925	-	53,305
Fair value revaluation of portfolio hedge	-	-	-	-	-	-	-
Financial assets held to maturity	-	-	-	-	-	-	-
Tax assets	-	-	0	-	-	69	69
Accruals and other assets	-	26	14	-	8	-	48
TOTAL	1,721	7,929	8,930	12,744	26,446	69	57,839

	12/31/2017					
	Total broken down	Accrued interest	Fair value adjustment	Impairment	Total	
Central banks	1,706	-	-	-	1,706	
Derivatives	-	637	3,992	-	4,629	
Financial assets available for sale	1,846	14	188	-	2,048	
Loans and advances due from banks	865	1	1	-	867	
Loans and advances to customers	53,305	593	3,047	(53)	56,892	
Fair value revaluation of portfolio hedge	-	-	2,518	-	2,518	
Financial assets held to maturity	-	-	-	-	-	
Tax assets	69	-	-	-	69	
Accruals and other assets	48	-	-	-	48	
TOTAL	57,839	1,245	9,746	(53)	68,777	

7.5.2. Breakdown of liabilities, excluding equity

	12/31/2017						
	Sight	Less than 3 months	3 months to 1 year	1 to 5 years	More than 5 years	No fixed maturity	Total broken down
Central banks	-	-	-	-	-	-	-
Derivatives	-	-	-	-	-	-	-
Due to banks	-	200	587	2,465	1,569	-	4,821
Customer borrowings and deposits	-	-	-	-	-	-	-
Debt securities	-	1,722	2,002	17,662	28,201	-	49,587
Fair value revaluation of portfolio hedge	-	-	-	-	-	-	-
Tax liabilities	-	-	0	-	-	-	0
Accruals and other liabilities	-	723	-	40	60	-	823
Provisions	-	-	-	41	-	-	41
Subordinated debt	-	-	-	-	-	-	-
TOTAL	-	2,645	2,589	20,208	29,830	-	55,272

	12/31/2017				
	Total broken down	Accrued interest	Fair value adjustment	Total	
Central banks	-	-	-	-	
Derivatives	-	548	7,386	7,934	
Due to banks	4,821	0	-	4,821	
Customer borrowings and deposits	-	-	-	-	
Debt securities	49,587	741	2,570	52,898	
Fair value revaluation of portfolio hedge	-	-	883	883	
Tax liabilities	0	-	-	0	
Accruals and other liabilities	823	(0)	-	823	
Provisions	41	-	-	41	
Subordinated debt	-	-	-	-	
TOTAL	55,272	1,289	10,839	67,400	

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7.5.3. Net balance sheet sensitivity gap

	12/31/2017					No fixed maturity	Total not broken down	Total
	Sight	Less than 3 months	3 months to 1 year	1 to 5 years	More than 5 years			
AMOUNT	1,721	5,284	6,341	(7,464)	(3,384)	69	(1,190)	1,377

7.6 - CURRENCY RISK

Classification by original currency	12/31/2016				
	EUR	Other currencies Europe	USD	Other currencies	Total
Total assets	69,688	2,255	1,576	1,588	75,107
Total liabilities	69,688	2,255	1,576	1,588	75,107
NET BALANCE SHEET POSITION	-	-	-	-	-

Classification by original currency	12/31/2017				
	EUR	Other currencies Europe	USD	Other currencies	Total
Total assets	66,381	1,380	429	587	68,777
Total liabilities	66,381	1,380	429	587	68,777
NET BALANCE SHEET POSITION	-	-	-	-	-

Caisse Française de Financement Local takes no foreign exchange risk. Assets and liabilities originally in non-euro currencies are swapped against Euribor as soon as they are recognized on the balance sheet.

7.7 - SENSITIVITY TO INTEREST RATE RISK

To limit its impact, interest rate risk is hedged in two stages by Caisse Française de Financement Local:

- In the first stage, all the assets and the liabilities benefiting from the privilege which do not naturally have a floating rate are hedged against Euribor until maturity as soon as they are recorded on the balance sheet. In practice, acquisitions of loan portfolios (in which the unit amount is generally small) are usually macro-hedged. Loans granted individually or bond issues can be micro- or macro-hedged. Hedging of assets and liabilities is more often obtained in using new interest rate swaps, but the same effect can also be obtained whenever possible by the cancelation of swaps of opposite direction;
- In the second stage, Euribor lending and borrowing flows (naturally or after hedges) are swapped against Eonia over a sliding period of maximum two years in order to eliminate the basis risk generated by differences in the tenor (Euribor 1, 3, 6 or 12 months) and the fixing risk due to re-fixing dates of reference indices that differ for the assets and the liabilities. The residual risk is managed using macro-hedges with a management horizon of one week.

These hedges can be entered into either directly on the market by Caisse Française de Financement Local, or through SFIL, which in turn hedges its resulting position in the market.

Non-privileged debt is not concerned by these hedging operations. In fact, debt contracted by Caisse Française de Financement Local with its shareholder to finance over-collateralization is borrowed either directly with a Eonia index and does not need to be swapped, or with a Euribor index and thus finances assets also indexed on Euribor. Short-term debt owed the Banque de France with a fixed rate (if any) is not hedged, but finances fixed rate assets.

The sensitivity of residual positions in fixed rates and variable rates fixed for a determined period of time that remain after the two levels of hedging is monitored on a monthly basis. Limits provide a framework for this sensitivity and are designed to reduce the impact on the value of balance sheet items in the event of a shift in the yield curve or a move in sloping/rotation. They are calibrated so as not to lose more than 6% of equity (i.e. EUR 80 million) with a quantile of 99% calculated based on 2007-2017 historical data.

The net present value (NPV) sensitivity indicators are calculated for a rate shock of 100 x +1 basis point (bp), aiming to limit losses in value in the event of:

- a parallel yield curve shift (limit of EUR 25 million for a shock of 100 x 1bp) to limit the fixed rate or directional rate risk;
- sloping/rotation of the interest rate curve:
 - net present value sensitivity calculation and limiting by time bucket, using four buckets of distinct risks on the yield curve in order to limit risk between distant points on the curve (limit per bucket of EUR 10 million for a shock of 100 x 1bp);
 - net present value sensitivity in terms of absolute value calculation and limiting by time bucket, using four buckets of distinct risks on the yield curve in order to limit risk between near points on the curve, within each bucket (limit per bucket of EUR 20 million for a shock of 100 x 1bp).

Limiting directional risk**Directional risk**

Total sensitivity

	Limit	3/31/2017	6/30/2017	9/30/2017	12/31/2017
Sensitivity	25.0	(0.1)	(1.6)	1.0	1.5

Risk of slope between two distant points on the rate curve

Sum of sensitivities

	Limit	3/31/2017	6/30/2017	9/30/2017	12/31/2017
Short term	10.0	0.1	0.4	(1.7)	0.2
Medium term	10.0	2.0	(4.5)	(2.4)	(4.6)
Long term	10.0	(2.6)	1.5	3.8	3.1
Very long term	10.0	0.4	1.1	1.3	2.7

Risk of slope between two close points on the rate curve

Sum of sensitivities in absolute value

	Limit	3/31/2017	6/30/2017	9/30/2017	12/31/2017
Short term	20.0	3.3	7.8	10.2	11.6
Medium term	20.0	5.1	12.4	10.9	14.8
Long term	20.0	4.9	3.5	7.1	3.6
Very long term	20.0	5.3	5.6	6.5	6.9

8. POST-CLOSING EVENTS

No significant event that could have influence the Company's financial situation occurred since the closing on December 31, 2017.

Statutory auditors' report on the financial statements established under IFRS

Year ended December 31, 2017

This is a free translation into English of the statutory auditors' review report issued in French and is provided solely for the convenience of English speaking readers. This report should be read in conjunction with, and is construed in accordance with, French law and professional standards applicable in France.

To the Chief Executive Officer,

In our capacity as statutory auditors of Caisse Française de Financement Local (the "Company") and pursuant to your request, in the context of the wish of your Company to provide more extensive financial information to investors, we have audited the accompanying financial statements of Caisse Française de Financement Local for the year ended December 31, 2017, established in accordance with IFRS as adopted by the European Union.

These financial statements have been prepared under the responsibility of your management. Since they were not intended to be submitted to the shareholders, they were not validated by the Executive Board. Our role is to express an opinion on these financial statements, based on our audit.

We conducted our audit in accordance with professional standards applicable in France and the professional guidance issued by the French institute of statutory auditors (*Compagnie nationale des commissaires aux comptes*) relating to this engagement. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the annual financial statements are free of material misstatement. An audit includes examining, using sample testing techniques or other selection methods, evidence supporting the amounts and disclosures in the annual financial statements. An audit also includes evaluating the appropriateness of accounting policies used and significant accounting estimates made, as well as evaluating the overall financial statement presentation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

In our opinion, the financial statements present fairly, in all material respects, the assets and liabilities and the financial position of the Company as of year-end, and the results of its operations for the year then ended in accordance with IFRS as adopted by the European Union.

This report is governed by French law. The courts of France shall have exclusive jurisdiction over any claim, dispute or difference resulting from our engagement letter or the present report, or any related matters. Each party irrevocably waives its right to oppose any action brought before French courts, to claim that the action is being brought before an illegitimate court or that the courts have no jurisdiction.

Paris-La-Défense and Neuilly-sur-Seine, March 29, 2018

The statutory auditors

French original signed by:

ERNST & YOUNG et Autres
Vincent Roty

DELOITTE & ASSOCIÉS
Sylvie Bourguignon

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Assets

EUR millions	Notes	12/31/2015	12/31/2016	12/31/2017
Central banks	2.1	2,496	3,684	1,706
Government and public securities	2.2	3,866	4,015	4,091
Loans and advances due from banks	2.3	4,876	411	905
Loans and advances to customers	2.4	46,918	47,701	46,871
Bonds and other fixed income securities	2.5	3,562	3,869	3,401
Equities and other variable income securities		-	-	-
Investments in non-consolidated companies and other long-term investments		-	0	-
Investments in consolidated companies		-	-	-
Intangible assets		-	-	-
Property and equipment		-	-	-
Unpaid capital		-	-	-
Uncalled subscribed capital		-	-	-
Treasury stocks		-	-	-
Other assets	2.6	19	4	17
Accruals and other assets	2.7	3,297	3,214	2,723
TOTAL ASSETS	2.8	65,034	62,898	59,714

Liabilities

EUR millions	Notes	12/31/2015	12/31/2016	12/31/2017
Central banks		-	-	-
Due to banks	3.1	5,520	5,225	4,821
Customer borrowings and deposits		-	-	-
Debt securities	3.2	53,185	52,058	49,919
Other liabilities	3.3	1,570	1,406	797
Accruals and other liabilities	3.4	3,200	2,597	2,552
Provisions	3.5	203	189	173
Subordinated debt		-	-	-
Equity		1,356	1,423	1,452
Share capital	3.6	1,315	1,315	1,350
Additional paid-in capital	3.6	-	-	-
Reserves and retained earnings	3.6	71	41	72
Net income	3.6	(30)	67	30
TOTAL LIABILITIES	3.7	65,034	62,898	59,714

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Off-balance sheet items

EUR millions	Notes	12/31/2015	12/31/2016	12/31/2017
COMMITMENTS GRANTED	4.1	893	3,847	3,121
Financing commitments		893	3,847	3,118
Guarantees granted		-	-	-
Commitments on securities		-	-	-
Other commitments granted		-	-	3
COMMITMENTS RECEIVED	4.2	8,679	6,951	6,093
Financing commitments		50	50	50
Guarantees received		8,629	6,901	6,043
Commitments on securities		-	-	-
Forward commitments		-	-	-
Other commitments received		-	-	-
Foreign currency transactions	4.3	16,030	14,943	14,244
Interest rate derivatives	4.4	148,022	134,500	123,616

Income statement

EUR millions	Notes	2015	2016	2017
Interest income	5.1	2,808	3,513	963
Interest expense	5.1	(2,622)	(3,334)	(836)
Income from variable income securities		-	-	-
Commission income	5.2	0	-	3
Commission expense	5.2	(26)	(7)	(15)
Net gains (losses) on held for trading portfolio		0	(0)	0
Net gains (losses) on placement portfolio	5.3	21	(9)	3
Other banking income		0	0	0
Other banking expense		(0)	(0)	(0)
NET BANKING INCOME		181	163	118
General operating expenses	5.4	(96)	(98)	(105)
Depreciation and amortization		-	-	-
GROSS OPERATING INCOME		85	65	13
Cost of risk	5.5	(14)	18	22
INCOME FROM OPERATIONS		71	83	35
Gains or losses on fixed assets	5.6	(5)	-	-
INCOME BEFORE NON-RECURRING ITEMS AND TAXES		66	83	35
Non-recurring items		-	-	-
Income tax	5.7	(96)	(16)	(5)
Net allocation to regulated provisions		-	-	-
NET INCOME		(30)	67	30
Basic earnings per share		(2.30)	5.08	2.20
Diluted earnings per share		(2.30)	5.08	2.20

Equity

EUR millions	Amount
AS OF 12/31/2016	
Share capital	1,315
Additional paid-in capital	-
Commitments to increase share capital and additional paid-in capital	-
Reserves and retained earnings	41
Net income for the year	67
Interim dividends	-
EQUITY AS OF 12/31/2016	1,423
MOVEMENTS FOR THE PERIOD	
Changes in share capital	35
Changes in additional paid-in capital	-
Changes in commitments to increase share capital and additional paid-in capital	-
Changes in reserves and retained earnings	66
Dividends paid (-)	(35)
Net income for the period	(37)
Other movements	-
AS OF 12/31/2017	
Share capital	1,350
Additional paid-in capital	-
Commitments to increase share capital and additional paid-in capital	-
Reserves and retained earnings	72
Net income for the period	30
EQUITY AS OF 12/31/2017	1,452

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Cash flow statement

EUR millions	2015	2016	2017
NET INCOME BEFORE TAXES	66	83	35
+/- Depreciation and write-downs	39	(23)	(40)
+/- Expense / income from operating activities	141	85	146
+/- Expense / income from financing activities	(184)	(59)	(99)
+/- Other items	130	308	24
= Non monetary elements included in net income before tax and other adjustments	126	311	31
+/- Cash from interbank operations	1,158	4,177	(883)
+/- Cash from customer operations (loans)	(772)	(962)	620
+/- Cash from customer financing assets	3,222	(520)	313
+/- Cash from hedging financial instruments	(1,258)	(731)	(607)
- Income tax paid	(35)	(17)	(29)
= Decrease / (increase) in cash from operating activities	2,315	1,947	(586)
CASH FLOW FROM OPERATING ACTIVITIES (A)	2,507	2,341	(520)
CASH FLOW FROM INVESTING ACTIVITIES (B)	-	-	-
+/- Cash from or for shareholders	-	-	(0)
+/- Other cash from financing activities	(540)	(1,148)	(1,452)
CASH FLOW FROM FINANCING ACTIVITIES (C)	(540)	(1,148)	(1,452)
EFFECT OF EXCHANGE RATES CHANGES ON CASH (D)	-	-	-
Increase / (decrease) in cash equivalents (A + B + C + D)	1,967	1,193	(1,972)
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	533	2,500	3,693
Central banks (assets and liabilities)	519	2,496	3,684
Interbank accounts (assets and liabilities) and loans / deposits at sight	14	4	9
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	2,500	3,693	1,721
Central banks (assets and liabilities)	2,496	3,684	1,706
Interbank accounts (assets and liabilities) and loans / deposits at sight	4	9	15
NET CHANGE IN CASH	1,967	1,193	(1,972)

Notes to the French GAAP financial statements

1. Significant accounting and valuation policies

1.1 – CONTEXT OF PUBLICATION

The financial statements as of December 31, 2017, were examined by the Executive Board on March 26, 2018.

1.2 – APPLICABLE ACCOUNTING STANDARDS: RULES ADOPTED BY THE AUTORITÉ DES NORMES COMPTABLES (ANC)

Caisse Française de Financement Local prepares its annual financial statements in compliance with ANC regulation n° 2014-07 issued on November 26, 2014, related to the annual accounts for the banking sector.

The financial statements as of December 31, 2017, were prepared using the same accounting principles as those used in the financial statements as of December 31, 2016.

The financial statements have been prepared in accordance with French generally accepted accounting principles, respecting the principles of prudence, sincerity and faithful image on the basis of the following assumptions:

- going concern principle,
- segregation of accounting periods,
- consistency of methods,
- historical costs,
- no netting principle,
- intangibility of the opening balance sheet.

The accounts are in accordance with the indications of directive 86/635/EEC of the Council of European Communities.

1.3 – ACCOUNTING PRINCIPLES APPLIED TO THE FINANCIAL STATEMENTS

1.3.1. Loans and advances to banks and to customers

Loans and advances to banks include all loans connected with banking operations except for those materialized by a security. They are broken down into sight accounts and term accounts. They include loans to SFIL refinancing export credit transactions.

Loans and advances to customers comprise loans granted to local governments.

They are recorded in the balance sheet net of impairment for possible loss. The undrawn portion of signed loan agreements is recorded as an off-balance sheet item.

Interest on loans is recorded as Interest income, *pro rata temporis* for accrued amounts as is interest on past-dues.

Commissions received and transaction costs related to the granting or the acquisition of a loan, if they are significant, are amortized over the maturity of the loan. Other commission income is recorded in the income statement on a cash basis.

Early loan reimbursement indemnities are recorded in the income statement at the date they occur, in accordance with article 2526-1 of ANC regulation 2014-07.

A loan is considered as non-performing when it presents one of the following characteristics:

- a probable or certain risk that it will not be repaid (past-due for more than nine months for local government borrowers, and for more than three months for the other counterparties);
- the existence of a factual counterparty risk (worsening of the financial situation, alert procedures).

Compromised non-performing loans are loans to borrowers whose recovery outlook is so downgraded that they are written off. Loans unpaid for more than one year are recorded in this category. Impairment charges are recorded for non-performing and compromised non-performing loans:

- The fraction of capital impaired is determined by Risk management in function of incurred losses. Underlying impairment charges and reversals are recognized as “Cost of risk” as well as the losses and subsequent recoveries on the principal of non-recoverable loans.
- Interest on non-performing and compromised non-performing loans is fully impaired. Underlying impairment charges and reversals are recognized as “Net interest margin” as well as the losses and subsequent recoveries on the interest of non-recoverable loans.

1.3.2. Securities

The securities held by Caisse Française de Financement Local are recorded in the assets as:

- Government and public entity securities eligible for central bank refinancing;
- Bonds and other fixed income securities.

The item Government and public entity securities eligible for central bank refinancing includes debt securities issued by public sector entities that may be refinanced through the European system of central banks.

The item Bonds and other fixed income securities includes the following categories of securities:

- debt securities issued by public sector entities that are not eligible for refinancing by central banks;
- debt securities guaranteed by public sector entities.

They are recognized for accounting purposes as investment securities or placement securities.

1.3.2.1. Investment securities

Fixed income securities with a determined maturity are recorded as investment securities when there is the intention and the capacity to hold them to maturity. Securities in this category are subject to backed financing or interest-rate hedging over their residual maturity.

Investment securities are recorded on the date of purchase at acquisition clean price excluding fees. Accrued interest at the date of acquisition is recorded as other assets. Interest on these securities is recorded in income as Interest income.

The difference between the redemption value and the acquisition clean cost (discount or premium) is amortized according to a quasi-actuarial method over the residual maturity of the security.

At the end of the reporting period, unrealized gains are not recorded and unrealized losses are not recognized except in the following cases:

- a doubt about the issuer's ability to meet their obligations;
- the probability that the Company will not hold these securities until maturity due to new circumstances.

1.3.2.2. Placement securities

Securities that do not fit in investment securities are recognized as placement securities.

Placement securities are recorded on the date of purchase at acquisition price excluding fees. Accrued interest at the date of acquisition is recorded as other assets. Interest on these securities is recorded as Interest income.

The difference between the redemption value and the acquisition clean cost (discount or premium) is amortized according to a quasi-actuarial method over the residual maturity of the security.

In application of the principle of prudence, placement securities are recorded on the balance sheet at their acquisition cost or selling price at closing, whichever is lower, after accounting, when relevant, for the value of the micro-hedge swap.

If the market for a financial instrument is not active, valuation techniques are used to calculate its selling price. The valuation model should take into account all the factors that market players would consider to value the asset. Within this framework, Caisse Française de Financement Local relies on its own valuation models, making every effort to take into account the market conditions at the date of the valuation as well as any changes in the credit quality of these financial instruments and market liquidity.

When the decrease in the value of the security exceeds the unrealized gain on the micro-hedge, the decrease in net value is recorded as asset impairment in Net gains (losses) on placement portfolio transactions, as well as impairment reversals and capital gains and losses on sales.

Placement securities transferred to investment securities are recorded at their acquisition cost and previously recognized impairment is reversed over the residual maturity of the securities concerned.

1.3.3. Debt due to banks

Debt due to banks is broken down according to the type of debt (sight accounts, current accounts, long-term loans or non-allocated receivables) and the initial maturity (sight or term debt).

Interest accrued on this debt is recorded in liabilities, offsetting net income.

1.3.4. Debt securities

Debt securities include *obligations foncières* and other resources benefiting from the privilege defined in article L.513-11 of the Monetary and Financial Code.

1.3.4.1. Obligations foncières

These debt securities are recorded at nominal value.

Redemption and issue premiums are amortized according to a quasi-actuarial method over the maturity of the securities *prorata temporis*. They are recorded on the balance sheet in the same categories as the corresponding debt. Amortization of these premiums is recorded in the income statement as Interest expense. If bonds are issued above par, amortization of issue premiums is deducted from Interest expense.

Interest on bonds is recorded in the interest margin as Interest income for accrued amounts calculated *prorata temporis*.

Bond issue costs and commissions are amortized according to a quasi-actuarial method over the maturity of the related bonds and are recorded in the interest margin as Interest expense.

Bonds denominated in foreign currencies are accounted for by the same method as foreign currency transactions (see below).

1.3.4.2. Registered covered bonds

They are private placements that are recorded at their nominal value. Applied accounting principles are identical to those used for *obligations foncières* (see above).

1.3.5. Provisions

Provisions are recorded based on their discounted value when the three following conditions are met:

- Caisse Française de Financement Local has a present legal or constructive obligation as a result of past events;
- it is probable that an outflow of resources representing economic benefits will be required to settle the obligation;
- a reliable estimate of the amount of the obligation can be made.

1.3.6. Derivative transactions

Caisse Française de Financement Local engages in derivative transactions only to hedge the interest rate and foreign exchange risks to which it is exposed in its activity. Depending on their purpose, these transactions are assigned to micro-hedge or macro-hedge portfolios. Valuation methods and accounting principles are determined according to the portfolio to which they are assigned.

Pursuant to article L.513-10 of the Monetary and Financial Code, these transactions benefit from the privilege defined in article L.513-11 of the Monetary and Financial Code provided that their purpose is to hedge the assets or debt benefiting from the privilege and the overall risk on the assets, liabilities and off-balance sheet items. The law stipulates that derivative transactions do not benefit from the privilege when related to sources of financing that do not benefit from the privilege. For Caisse Française de Financement Local, the only resources that do not benefit from the privilege comprise the debt contracted from SFIL and Caisse Française de Financement Locas's equity, which are not hedged.

The notional amount of these hedging transactions is recorded as an off-balance sheet item over the maturity of the contract, i.e. from the date the contract is signed (including forward contracts) up to maturity. The amount recorded is adjusted to reflect any changes in notional amounts so as to represent the maximum current or future commitment.

Payments at the inception of hedging derivatives are amortized over their maturity for the time remaining according to a quasi-actuarial method.

1.3.6.1. Micro-hedge transactions

Derivatives are booked as micro-hedges when they are designed to hedge against the interest rate risk or the foreign exchange risk related to an item or set of homogeneous items identified from the outset. They involve swaps used to hedge issues of debt securities and certain loans and advances to customers.

Expense and income on these transactions are recorded in the income statement in the same way income and expense on the hedged item or set of homogeneous items are recorded.

Termination fees received or paid because of the early interruption of the hedging instrument are recorded in the income statement at the termination date, in accordance with article 2526-1 of ANC regulation 2014-07.

1.3.6.2. Macro-hedge transactions

This category includes transactions designed to hedge and manage the Company's overall exposure to interest rate risk on assets, liabilities and off-balance sheet items, excluding micro-hedge transactions. They were authorized on December 1, 1999, by a specific decision of the Executive Board of Caisse Française de Financement Local.

Expense and income on these transactions are recorded in the income statement *prorata temporis* respectively as Interest expense and Interest income. The counterpart is recorded in accruals until the payment date.

If an early reimbursement of a loan leads to the cancellation of macro-hedge swaps, the swap termination fee is recorded in the income statement at the termination date.

1.3.7. Foreign currency transactions

Caisse Française de Financement Local records foreign currency transactions in accounts opened and denominated in each of the currencies used.

Specific foreign exchange position accounts and foreign exchange position equivalent accounts are opened in each currency.

At the end of each reporting period, differences between on the one hand the amounts resulting from a market price valuation of the foreign exchange position accounts and on the other hand the amounts recorded in the foreign exchange position equivalent accounts are recorded in the income statement.

1.3.8. Foreign exchange transactions

In the course of systematic hedging of its foreign exchange risk, Caisse Française de Financement Local enters into currency swaps. These currency swaps are initiated to eliminate the risk of foreign exchange rate fluctuations that might affect an asset or liability as soon as such a risk is recognized. They are mainly used to hedge certain bond issues, debt securities and customer loans.

Results of foreign exchange hedging transactions are accounted for by recording the difference between the hedging rate and the spot rate – contango or backwardation – *prorata temporis* in the income statement.

1.3.9. Guarantees

As part of its activity to refinance large export credits, Caisse Française de Financement Local benefits from an irrevocable and unconditional 100% guarantee by the French State, called an enhanced guarantee. Expenses related to these guarantees are recorded *prorata temporis* in the interest margin as Interest expense.

1.3.10. Non-recurrent income and expense

Non-recurrent income and expense result from events or transactions that do not relate to ordinary business operations or routine management of the Company's assets and liabilities.

Furthermore, the income or expense involved does not depend on decisions taken within the framework of usual management of the Company's activities or assets, but results from external events of a completely exceptional nature. Only items of this nature that have a significant impact on the period's net income are recorded as non-recurrent income and expense.

1.3.11. Tax consolidation

Since January 1, 2014, Caisse Française de Financement Local belongs to the tax group that is headed up by SFIL. This entity pays the total income tax owed by the Group. Caisse Française de Financement Local records in its accounts the amount of tax for which it would be liable if it were not a member of the tax group.

Tax savings realized by the tax group are recorded in the accounts of SFIL.

1.3.12. Offices and activities in uncooperative States and territories

In application of article L.511-45 of the Monetary and Financial Code, it should be noted that Caisse Française de Financement Local has no offices in States that have not signed an administrative assistance agreement with France (subsidiaries, branches, including *ad hoc* entities, and equity interest in other entities over which the Company has exclusive or joint (or *de facto*) control).

1.3.13. Identity of the parent company consolidating the accounts of Caisse Française de Financement Local as of December 31, 2017

SFIL
1-3 rue du Passeur de Boulogne
92130 Issy-les-Moulineaux

2. NOTES TO THE ASSETS (EUR millions)

2.1 - CENTRAL BANKS

	12/31/2015	12/31/2016	12/31/2017
Mandatory reserves	-	-	-
Other deposits	2,496	3,684	1,706
TOTAL	2,496	3,684	1,706

2.2 - GOVERNMENT AND PUBLIC ENTITY SECURITIES ELIGIBLE FOR CENTRAL BANK REFINANCING

2.2.1. Accrued interest included in this item: 53

2.2.2. Analysis by residual maturity excluding accrued interest

Less than 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
55	158	881	2,944	4,038

2.2.3. Analysis by listed securities and other securities excluding accrued interest

	Amount as of 12/31/2015	Amount as of 12/31/2016	Amount as of 12/31/2017	Impairment as of 12/31/2017	Unrealized capital gain or loss as of 12/31/2017 ⁽²⁾
Listed securities ⁽¹⁾	3,501	3,664	3,755	(0)	(869)
Other securities	309	293	283	-	(44)
TOTAL	3,810	3,957	4,038	(0)	(913)

(1) Listed securities are registered for trading on a stock exchange.

(2) The unrealized capital gain or loss is calculated as the difference between the book value and the market value, taking derivatives into account.

2.2.4. Analysis by type of portfolio excluding accrued interest and changes during the year

Portfolio	Net amount as of 12/31/2015	Net amount as of 12/31/2016	Gross amount as of 12/31/2016	Acquisitions	Amortization, redemption or disposals	Transfers	Subtotal as of 12/31/2017
Trading	-	-	-	-	-	-	-
Placement	685	925	925	444	(293)	-	1,076
Investment	3,125	3,032	3,032	-	(67)	-	2,965
TOTAL	3,810	3,957	3,957	444	(360)	-	4,041

Portefeuille	Subtotal as of 12/31/2017	Translation adjustments	Impairment as of 12/31/2017	Net amount as of 12/31/2017 ⁽¹⁾	Unrealized capital gain or loss as of 12/31/2017 ⁽²⁾
Trading	-	-	-	-	-
Placement	1,076	-	(0)	1,076	(27)
Investment	2,965	(3)	-	2,962	(886)
TOTAL	4,041	(3)	(0)	4,038	(913)

(1) This amount includes a premium / discount of EUR 21 million for the placement portfolio and of EUR 121 million for the investment portfolio.

(2) The unrealized capital gain or loss is calculated as the difference between the book value and the market value, taking derivatives into account.

2.2.5. Impairment breakdown by country

See note 2.9

2.3 - LOANS AND ADVANCES DUE FROM BANKS

2.3.1. Sight loans and advances due from banks

	12/31/2015	12/31/2016	12/31/2017
Sight accounts	4	4	10
Unallocated sums	0	7	13
TOTAL	4	11	23
of which replacement assets	4	4	10

2.3.2. Term loans and advances due from banks

2.3.2.1. Accrued interest included in this item: 2

2.3.2.2. Analysis by residual maturity excluding accrued interest

Less than 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
123	404	93	260	880

2.3.2.3. Analysis by initial maturity excluding accrued interest

	Net amount as of 12/31/2015	Net amount as of 12/31/2016	Gross amount as of 12/31/2017	Decrease in value as of 12/31/2017	Net amount as of 12/31/2017
Loans of less than 1 year	-	-	-	-	-
Loans of more than 1 year	4,865	397	880	-	880
TOTAL	4,865	397	880	-	880

2.3.2.4. Breakdown by counterparty

	12/31/2015	12/31/2016	12/31/2017
SFIL - Export credits refinancing loans guaranteed by the French State ⁽¹⁾	-	-	218
SFIL - Others loans ⁽²⁾	2,339	-	360
Swiss cantonal banks benefiting from their cantons' legal guarantee	355	107	29
Banks guaranteed by a local government, <i>crédits municipaux</i>	56	32	21
Other credit institutions of which loans benefiting from the assignment in guarantee of refinanced public debt	2,115	258	252
TOTAL	4,865	397	880
<i>of which replacement assets</i>	<i>2,339</i>	<i>-</i>	<i>360</i>

(1) In 2017, Caisse Française de Financement Local granted loans to its parent company, SFIL, to refinance large export credits granted by SFIL. These loans benefit from an irrevocable and unconditional 100% guarantee by the French State, known as enhanced guarantee.

(2) In 2017, Caisse Française de Financement Local invested some of its surplus cash in loans granted to its parent company SFIL.

2.4 - CUSTOMER LOANS AND ADVANCES**2.4.1. Accrued interest included in this item: 530****2.4.2. Analysis by residual maturity excluding accrued interest**

Less than 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
1,373	3,007	14,316	27,645	46,341

2.4.3. Analysis of commitments by the counterparty's economic sector excluding accrued interest

Economic sector	12/31/2015	12/31/2016	12/31/2017 ⁽¹⁾
Public sector	43,480	44,646	44,173
Other sectors	2,795	2,483	2,168
TOTAL	46,275	47,129	46,341

(1) Of which EUR 38,865 million eligible for central bank refinancing.

2.4.4. Analysis by initial maturity excluding accrued interest

	Net amount as of 12/31/2015	Net amount as of 12/31/2016	Gross amount as of 12/31/2017	Impairment as of 12/31/2016	Net amount as of 12/31/2017
Loans of less than 1 year	6	5	5	-	5
Loans of more than 1 year	46,269	47,124	46,372	(36)	46,336
TOTAL	46,275	47,129	46,377	(36)	46,341

2.4.5. Analysis of loans by category of outstanding loans excluding accrued interest

	Net amount as of 12/31/2015	Net amount as of 12/31/2016	Gross amount as of 12/31/2017	Impairment as of 12/31/2017	Net amount as of 12/31/2017
Performing commitments	45,682	46,645	45,828	-	45,828
Non-performing loans	274	205	279	(6)	273
Compromised non-performing loans	319	279	270	(30)	240
TOTAL	46,275	47,129	46,377	(36)	46,341

Assets considered as forborne by Caisse Française de Financement Local concern exposures to loan contracts for which concessions have been granted in light of the borrower's financial difficulties (recognized or to come) that would not have been granted in other circumstances. These concessions may either be a waiver of a part of the debt, a rescheduling of the loan repayment, restructuring measures through an amendment to the loan contract, or a partial or full refinancing of the loan with a new contract, including for transactions targeting the reduction of the sensitivity of the loan.

There were 211 forborne contracts as of December 31, 2017, with 108 borrowers, for a total of EUR 1,364 million.

2.4.6. Depreciation for non-performing loans - changes during the year

	12/31/2015	12/31/2016	Allocations	Reversals	Transfers	12/31/2017
For non-performing loans						
On loans	(2)	(3)	-	3	-	(0)
On interest	(12)	(8)	(5)	7	-	(6)
For compromised non-performing loans						
On loans	(4)	(2)	(0)	2	-	(0)
On interest	(48)	(47)	(15)	32	-	(30)
TOTAL	(66)	(60)	(20)	44	-	(36)

Provisions on interest are recorded in Net banking income and provisions on nominal are recorded in Cost of risk.

2.4.7. Impairment breakdown by country

See note 2.9

2.5 - BONDS AND OTHER FIXED INCOME SECURITIES**2.5.1. Accrued interest included in this item: 24****2.5.2. Analysis by residual maturity excluding accrued interest**

Less than 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
-	158	750	2,469	3,377

2.5.3. Analysis by the issuer's economic sector excluding accrued interest

	12/31/2015	12/31/2016	12/31/2017
Public sector	3,076	2,865	2,550
Other sectors (guaranteed by a State or by a local government)	463	335	246
Credit institutions	-	646	581
TOTAL	3,539	3,846	3,377
<i>of which eligible for central bank refinancing</i>	52	548	629
<i>of which replacement assets</i>	-	646	581

2.5.4. Analysis by listed securities and other securities excluding accrued interest

	Amount as of 12/31/2015	Amount as of 12/31/2016	Amount as of 12/31/2017	Impairment as of 12/31/2017	Unrealized capital gain or loss as of 12/31/2017 ⁽¹⁾
Listed securities	1,345	1,828	1,563	(0)	(26)
Other securities	2,194	2,018	1,814	-	(182)
TOTAL	3,539	3,846	3,377	(0)	(208)

(1) The unrealized capital gain or loss is after swap and corresponds to the difference between accounting value and market value.

2.5.5. Analysis by type of portfolio excluding accrued interest and changes during the year

Portfolio	Net amount as of 12/31/2015	Net amount as of 12/31/2016	Gross amount as of 12/31/2016	Acquisitions	Amortization, redemption or disposals	Transfers	Subtotal as of 12/31/2017
Trading	-	-	-	-	-	-	-
Placement	570	1,093	1,093	560	(702)	-	951
Investment	2,969	2,753	2,753	-	(262)	-	2,491
TOTAL	3,539	3,846	3,846	560	(964)	-	3,442

Portfolio	Subtotal as of 12/31/2017	Translation adjustments	Impairment as of 12/31/2017	Net amount as of 12/31/2017 ⁽¹⁾	Unrealized capital gain or loss as of 12/31/2017 ⁽²⁾
Trading	-	-	-	-	-
Placement	951	(31)	(0)	920	4
Investment	2,491	(34)	-	2,457	(212)
TOTAL	3,442	(65)	(0)	3,377	(208)

(1) These amounts include a premium / discount of EUR 16 million for placement portfolio and of EUR 86 million for investment portfolio.

(2) The unrealized capital gain or loss is calculated as the difference between the book value and the market value, taking derivatives into account.

2.5.6. Breakdown of impairment by country

See note 2.9

2.6 - OTHER ASSETS

	12/31/2015	12/31/2016	12/31/2017
Other receivables	19	4	17
TOTAL	19	4	17

2.7 - ACCRUALS AND OTHER ASSETS

	12/31/2015	12/31/2016	12/31/2017
Deferred losses on hedging transactions	1,873	1,624	1,472
Deferred charges on bond issues	41	45	48
Prepaid charges on hedging transactions	223	182	183
Premiums on acquisition of loans	182	240	256
Other prepaid charges	0	-	-
Accrued interest not yet due on hedging transactions	977	897	748
Translation adjustments	-	210	-
Other deferred income	-	0	1
Other accruals	1	16	15
TOTAL	3,297	3,214	2,723

2.8 - TOTAL ASSETS

Analysis by original currency	Amount in original currency as of 12/31/2015	Amount in euros as of 12/31/2015	Amount in original currency as of 12/31/2016	Amount in euros as of 12/31/2016	Amount in original currency as of 12/31/2017	Amount in euros as of 12/31/2017
EUR	59,436	59,436	58,063	58,063	57,725	57,725
AUD	20	14	20	14	20	13
CAD	1,017	674	965	681	511	340
CHF	1,896	1,746	1,497	1,396	1,035	884
GBP	637	867	318	372	129	145
HKD	201	24	201	25	0	0
JPY	95,050	726	91,934	747	21,168	157
NOK	1,039	108	1,039	114	1,039	105
PLN	39	9	41	9	43	10
SEK	0	0	0	0	0	0
USD	1,556	1,430	1,556	1,477	402	335
TOTAL		65,034		62,898		59,714

2.9 - BREAKDOWN OF IMPAIRMENT BY COUNTRY

	Amount as of 12/31/2015	Amount as of 12/31/2016	Amount as of 12/31/2017
Government and public entity - placement securities	-	(0)	(0)
France	-	(0)	(0)
Bonds and other fixed income - placement securities	-	(0)	(0)
France	-	(0)	(0)
Belgium	-	-	(0)
Norway	-	-	(0)
Sweden	-	-	(0)
Bonds and other fixed income - investment securities	-	-	-
Loans and advances to customers	(66)	(60)	(36)
France	(66)	(60)	(36)

2.10 - BREAKDOWN OF GOVERNMENT BONDS IN A SELECTION OF EUROPEAN COUNTRIES

The reported credit risk exposure represents the accounting net carrying amount, being the notional amounts after deduction of specific impairments and recording of accrued interest.

	12/31/2016					Total
	Spain	Ireland	Italy	Portugal	Greece	
Investment securities	-	-	458	-	-	458
Placement securities	201	-	113	-	-	314
TOTAL	201	-	571	-	-	772

	12/31/2017					Total
	Spain	Ireland	Italy	Portugal	Greece	
Investment securities	-	-	451	-	-	451
Placement securities	203	-	112	-	-	315
TOTAL	203	-	563	-	-	766

3. NOTES TO THE LIABILITIES (EUR millions)

3.1 - DUE FROM BANKS

At the end of December 31, 2017, funding obtained from SFIL, within the framework of the financing agreement, was comprised of different loans with maturities initially between one day and ten years, indexed on Euribor or Eonia.

	12/31/2015	12/31/2016	12/31/2017
Sight accounts	-	-	-
Current account - parent company	-	-	-
Interest accrued not yet due	-	-	-
Term borrowing - parent company	5,511	5,220	4,821
Interest accrued not yet due	9	5	0
Unallocated sums	-	-	-
TOTAL	5,520	5,225	4,821

Analysis by residual maturity excluding accrued interest

	Less than 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total as of 12/31/2017
Sight	-	-	-	-	-
Term	200	587	2,465	1,569	4,821
TOTAL	200	587	2,465	1,569	4,821

3.2 - DEBT SECURITIES

3.2.1. Debt securities (*obligations foncières*)

3.2.1.1. Accrued interest included in this item: 592

3.2.1.2. Analysis by residual maturity excluding accrued interest

Type of securities	Less than 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
<i>Obligations foncières</i>	1,664	1,954	17,224	21,877	42,719
<i>of which net issue premiums ⁽¹⁾</i>	(0)	(0)	(10)	(65)	(75)

(1) The gross amount of positive and negative issue premiums totaled EUR - 162 million before amortization.

3.2.1.3. Changes during the year excluding accrued interest

Type of securities	12/31/2016	Increase	Decrease	Translation adjustment	12/31/2017
<i>Obligations foncières</i>	44,885	5,526	(7,520)	(172)	42,719

3.2.2. Other bonds (registered covered bonds)**3.2.2.1. Accrued interest included in this item: 149****3.2.2.2. Analysis by residual maturity excluding accrued interest**

Type of securities	Less than 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
Registered covered bonds	58	48	282	6,071	6,459
of which net issue premiums ⁽¹⁾	-	-	(0)	44	44

(1) The gross amount of positive and negative issue premiums totaled EUR 50 million before amortization.

3.2.2.3. Changes during the year excluding accrued interest

Type of securities	12/31/2016	Increase	Decrease	Translation adjustment	12/31/2017
Registered covered bonds	6,294	451	(286)	-	6,459

3.3 - OTHER LIABILITIES

	12/31/2015	12/31/2016	12/31/2017
Cash collateral received	1,397	1,263	687
Accrued interest not yet due on cash collateral received	0	(0)	(0)
Taxes	11	7	0
Balances to pay on unwound hedging contracts	-	-	-
Contribution to the support fund ⁽¹⁾	162	136	110
Other creditors	-	0	0
TOTAL	1,570	1,406	797

(1) This item represents the commitments taken by Caisse Française de Financement Local to contribute to the pluri-annual support funds:

- in 2013, for local governments in the amount of EUR 10 million for 15 years (EUR 150 million);

- in 2014 and 2015 for public hospitals in the amount of respectively EUR 18 million (EUR 6 million for three years) and EUR 20 million (EUR 10 million for two years).

3.4 - ACCRUALS AND OTHER LIABILITIES

	12/31/2015	12/31/2016	12/31/2017
Deferred gains on hedging transactions	-	-	-
Deferred income on hedging transactions	2,165	1,710	1,569
Deferred income on loans	166	151	160
Accrued interest not yet due on hedging transactions	836	717	658
Other accrued charges	15	16	24
Translation adjustments	18	-	139
Other accruals	-	3	2
TOTAL	3,200	2,597	2,552

3.5 - PROVISIONS FOR RISKS AND CHARGES

	12/31/2015	12/31/2016	Increase	Decrease	Translation adjustment	12/31/2017
Loans, commitments ⁽¹⁾	64	46	1	(17)	-	30
Financial instruments	24	34	-	(4)	-	30
Other provisions ⁽²⁾	115	109	4	-	-	113
TOTAL	203	189	5	(21)	-	173

(1) In 2016 and 2017, Caisse Française de Financement Local reduced its collective provisions, linked to its loans to customers by reason of the progress made in its policy of reducing the sensitivity of its structured loans.

(2) For the record, in 2015, French tax authorities investigated the income declared and the tax paid for 2012 and 2013. Following the tax assessment, the tax authorities expressed their disagreement with the tax treatment of the following two points: the taxation in Ireland of the income from the Dublin branch of Dexia Municipal Agency, which is now closed, and the deductibility of provisions for non-performing loans. In order to safeguard its rights to the disputed adjustment, in 2017 the tax authority initiated a verification procedure relating to the consequences of its previous assessment of taxable income for the 2014 to 2016 fiscal years. The two points of disagreement resulting from the 2015 assessment still held following this tax audit. There were no other new developments.

In 2016 and 2017, Caisse Française de Financement Local started an appeal within the framework of legal recourse allowed by current tax regulations. In 2017, provision recorded in 2015 was adjusted for due interest.

3.6 - EQUITY

	12/31/2015	12/31/2016	12/31/2017
Share capital	1,315	1,315	1,350
Legal reserve	46	46	49
Retained earnings (+/-)	25	(5)	23
Net income (+/-)	(30)	67	30
TOTAL	1,356	1,423	1,452

On May 30, 2017, the Ordinary and Extraordinary Shareholders' Meeting decided to allocate the 2016 net profit, ie EUR 62 millions after taking into account of negative retained earnings, to Legal reserve for EUR 3 million and to payment of a dividend in the amount of EUR 35 million, the difference, amounting to EUR 24 million, was allocated to the retained earnings.

At the same date, the Extraordinary General Meeting of the Caisse Française de Financement Local decided to increase the share capital by an amount of EUR 35 million subscribed by SFIL, its parent company.

Caisse Française de Financement Local's share capital totaled EUR 1,350 million, comprising 13,500,000 shares.

3.7 - TOTAL LIABILITIES

Analysis by original currency	Amount in original currency as of 12/31/2015	Amount in euro as of 12/31/2015	Amount in original currency as of 12/31/2016	Amount in euro as of 12/31/2016	Amount in original currency as of 12/31/2017	Amount in euro as of 12/31/2017
EUR	59,436	59,436	58,063	58,063	57,725	57,725
AUD	20	14	20	14	20	13
CAD	1,017	674	965	681	511	340
CHF	1,896	1,746	1,497	1,396	1,035	884
GBP	637	867	318	372	129	145
HKD	201	24	201	25	0	0
JPY	95,050	726	91,934	747	21,168	157
NOK	1,039	108	1,039	114	1,039	105
PLN	39	9	41	9	43	10
SEK	0	0	0	0	0	0
USD	1,556	1,430	1,556	1,477	402	335
TOTAL		65,034		62,898		59,714

3.8 - TRANSACTIONS WITH RELATED PARTIES

Analysis by nature	Parent company ⁽¹⁾			Other related parties ⁽²⁾		
	12/31/2015	12/31/2016	12/31/2017	12/31/2015	12/31/2016	12/31/2017
ASSETS						
Loans and advances due from banks - sight	-	-	-	-	-	-
Loans and advances due from banks - term	2,341	-	578	-	-	-
Bonds and other fixed income securities	-	-	-	-	-	9
LIABILITIES						
Due to banks - sight	-	-	-	-	-	-
Due to banks - term	5,520	5,225	4,821	-	-	-
INCOME STATEMENT						
Interest income on loans and advances	11	6	1	(9)	(11)	(11)
Interest income on debt securities	-	0	-	-	0	0
Interest expense on borrowings	(37)	(25)	(11)	-	(0)	-
Net commissions	(19)	(3)	(11)	-	(0)	0
OFF-BALANCE SHEET						
Interest rate derivatives	17,499	13,858	14,029	-	-	-
Foreign exchange derivatives	4,137	3,478	1,271	-	-	-
Commitments and guarantees received	2,391	50	50	140	52	-
Commitments and guarantees given	600	3,722	3,028	-	-	-

(1) This item includes transactions with SFIL, the parent company of Caisse Française de Financement Local.

(2) This item may include transactions with Caisse des dépôts et consignations and La Banque Postale, shareholders of SFIL.

Management Report

Report on corporate governance

IFRS Financial Statements

French GAAP Financial Statements

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Shareholders' Meeting

General Information

4. NOTES TO THE OFF-BALANCE SHEET ITEMS (EUR millions)

4.1 - COMMITMENTS GRANTED

	12/31/2015	12/31/2016	12/31/2017
Financing commitments granted to credit institutions ⁽¹⁾	600	3,722	3,028
Financing commitments granted to customers ⁽²⁾	293	125	90
Other commitments given, assets assigned in guarantee ⁽³⁾	-	-	3
TOTAL	893	3,847	3,121

(1) Within the framework of the export credit business, this amount corresponds to a commitment by Caisse Française de Financement Local to refinance its parent company, SFIL.

(2) Financing commitments granted to customers correspond to contracts signed for loans not yet paid out to customers at year-end.

(3) It means the irrevocable payment commitment to the Fonds de garantie et de résolution.

4.2 - COMMITMENTS RECEIVED

	12/31/2015	12/31/2016	12/31/2017
Financing commitments received from credit institutions ⁽¹⁾	50	50	50
Currencies borrowed	-	-	-
Guarantees received from credit institutions	2,525	84	22
Enhanced guarantees ⁽²⁾	-	3,722	3,247
Guarantees received from local governments and asset transfers as guarantees of commitments on local governments	6,104	3,095	2,774
Other commitments received	-	-	-
TOTAL	8,679	6,951	6,093

(1) At the end of December 2017, this item corresponded to the amount of the overdraft, authorized in the current account agreement set up with SFIL, totaling EUR 50 million.

(2) The financing and financing commitments granted to SFIL by Caisse de Financement Local to refinance the former's large export credits benefit from a 100% unconditional and irrevocable guarantee of the French State, referred to as an enhanced guarantee.

4.3 - FOREIGN CURRENCY TRANSACTIONS

Cash and forward foreign exchange transactions are recorded at their value in foreign currencies translated at the exchange rate at the end of the period.

The items Currencies to receive and Currencies to deliver are composed of long currency swaps with intermediate payment flows corresponding to hedging transactions.

	12/31/2015	12/31/2016	12/31/2017	Fair value as of 12/31/2017
Currencies to receive	8,006	7,682	6,983	250
Currencies to deliver	8,024	7,472	7,122	(312)
TOTAL	16,030	15,154	14,105	(62)

4.4 - COMMITMENTS ON INTEREST RATE DERIVATIVES

Commitments on interest rate derivatives are recorded in accordance with CRB standards 88-02 and 90-15: amounts related to unconditional operations are recorded at the contractual notional value.

4.4.1. Analysis of over-the-counter interest rate transactions by residual maturity

Type of transaction	12/31/2016	Less than 1 year	1 year to 5 years	More than 5 years	12/31/2017
Notional amount	134,500	42,984	28,243	52,389	123,616
of which deferred start	3,345	400	3,055	502	3,957

These hedging transactions include micro-hedge and macro-hedge transactions.

4.4.2. Analysis of interest rate transactions by product type

	12/31/2015	12/31/2016	12/31/2017
Interest rate swaps	148,022	134,500	123,616
Term contracts	-	-	-
Interest rate options	-	-	-
TOTAL	148,022	134,500	123,616

4.4.3. Analysis of interest rate swap transactions

	12/31/2015	12/31/2016	12/31/2017	Fair value as of 12/31/2017
Micro-hedge	69,794	66,613	62,306	(667)
Macro-hedge	78,228	67,887	61,310	(2,436)
TOTAL	148,022	134,500	123,616	(3,103)

4.4.4. Analysis of interest rate transactions by counterparty

	12/31/2015	12/31/2016	12/31/2017
Related parties	17,499	13,858	14,029
Other counterparties	130,523	120,642	109,587
TOTAL	148,022	134,500	123,616

5. NOTES TO THE STATEMENT OF INCOME (EUR millions)**5.1 - INTEREST AND RELATED INCOME / EXPENSE**

	2016	2017
INCOME	3,513	963
Due from banks	23	9
Due from customers	3,388	1,029
Bonds and other fixed income securities	71	71
Macro-hedge transactions	31	(146)
Other commitments	-	-
EXPENSE	(3,334)	(836)
Due to banks	(35)	(20)
Due to customers	(2,410)	(273)
Bonds and other fixed income securities	148	(152)
Macro-hedge transactions	(1,037)	(391)
Other commitments	-	-
INTEREST MARGIN	179	127

5.2 - COMMISSIONS

	2016			2017		
	Income	Expense	Net	Income	Expense	Net
Lending activity	0	-	0	0	-	0
Purchase and sale of securities	-	(1)	(1)	-	(1)	(1)
Services on securities other than custodian services	-	(3)	(3)	-	(3)	(3)
Commissions on financial instruments	-	(0)	(0)	3	-	3
Rebiling by parent company	-	(3)	(3)	-	(11)	(11)
TOTAL	0	(7)	(7)	3	(15)	(12)

5.3 - ANALYSIS OF GAINS AND LOSSES ON PORTFOLIO TRANSACTIONS

	2016	2017
Transactions on placement securities ⁽¹⁾	(9)	3
Transactions on investment securities	-	-
Transactions on interest rate derivatives	-	-
Foreign exchange transactions	(0)	-
TOTAL	(9)	3

(1) This item regroups capital gains and losses on sales and provisions and reversals on this portfolio amount after swaps.

5.4 - GENERAL EXPENSES

Caisse Française de Financement Local has no salaried employees in accordance with article L.513-15 of the Monetary and Financial Code. The general management of the operations of Caisse Française de Financement Local has been entrusted by an agreement to its parent company, SFIL, a credit institution.

Specific individual agreements have been established with entities that have transferred assets to the société de crédit foncier, and continue to ensure management for their national clientele. These assets are managed in a run-off mode. At the end of 2017, there were agreements with the following entities: Kommunalkredit Austria (Austria), Belfius Banque et Assurances (Belgium), and Dexia Crediop (Italy). These agreements already existed in previous years. Starting in 2015, management of new registered covered bonds (RCB) is entrusted to Landesbank Baden-Württemberg (LBBW). Dexia Kommunalbank Deutschland continues to manage registered covered bonds issued prior to 2015.

General operating expense can be broken down as follows:

	2016	2017
Personnel cost	-	-
Other general operating expenses ⁽¹⁾	(91)	(98)
Taxes	(7)	(7)
TOTAL	(98)	(105)

(1) of which EUR 95 million with SFIL.

5.5 - COST OF RISK

	2016	2017
Collective and specific impairments	18	22
TOTAL	18	22

5.6 - GAINS AND LOSSES ON FIXED ASSETS

	2016	2017
Transactions on investment securities	-	-
Other transactions	-	-
TOTAL	-	-

5.7 - CORPORATE INCOME TAX

	2016	2017
Income tax for the year ⁽¹⁾	(22)	(2)
Provisions for tax litigation ⁽²⁾	6	(3)
TOTAL	(16)	(5)

(1) The corporate tax rate in France in 2017 is 34.43%, plus an additional tax of 15%.

(2) See note 3.5

6. POST-CLOSING EVENTS

No significant event that could have influence the Company's financial situation occurred since the closing on December 31, 2017.

Statutory Auditors' report on the financial statements

Year ended December 31, 2017

This is a translation into English of the statutory auditors' report on the financial statements of the Company issued in French and it is provided solely for the convenience of English speaking users.

This statutory auditors' report includes information required by European regulation and French law, such as information about the appointment of the statutory auditors or verification of the management report and other documents provided to shareholders.

This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.

To the Shareholder's Meeting of Caisse Française de Financement Local,

Opinion

In compliance with the engagement entrusted to us, we have audited the accompanying financial statements of Caisse Française de Financement Local for the year ended December 31, 2017.

In our opinion, the financial statements give a true and fair view of the assets and liabilities and of the financial position of the Company as of December 31, 2017 and of the results of its operations for the year then ended in accordance with French accounting principles.

The audit opinion expressed above is consistent with our report to the Financial Statements Committee of SFIL, the parent company of Caisse Française de Financement Local, and also acting as the Financial Statements Committee of the latter.

Basis for opinion

Audit framework

We conducted our audit in accordance with professional standards applicable in France. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the "Statutory auditors' Responsibilities for the Audit of the Financial Statements" section of our report.

Independence

We conducted our audit engagement in compliance with independence rules applicable to us, for the period from January 1, 2017 to the date of our report and specifically we did not provide any prohibited non-audit services referred to in article 5(1) of Regulation (EU) N°537/2014 or in the French Code of ethics (code de déontologie) for statutory auditors.

Justification of assessments - key audit matters

In accordance with the requirements of articles L.823-9 and R.823-7 of the French Code of Commerce (Code de commerce) relating to the justification of our assessments, we inform you of the key audit matters relating to risks of material misstatement that, in our professional judgment, were of most significance in our audit of the financial statements of the current period, as well as how we addressed those risks.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on specific items of the financial statements.

Credit risk related to French local communities

Considerations	Summary of planned audit procedure
<p>The loans and advances to customers is one of the largest items of the Caisse Française de Financement Local balance sheet as of December 31, 2017 appearing for a net amount of EUR 46,871 million. The outstanding amount of loans and receivables to French local communities alone represents main part of the credit stock. These loans and receivables to French local communities correspond mainly to loans acquired from La Banque Postale (LBP) and the remaining stock of loans from Dexia Credit Local's activities, including a portfolio of sensitive structured loans.</p> <p>As stated in the first note to annual financial statements, if there is an objective indication of deterioration of the credit risk, a specific depreciation is accounted for.</p> <p>As of December 31, 2017, the stock of specific impairment amounts to EUR 36 million.</p> <p>The Risks division of SFIL entity sets the policies, guidelines and procedures related to credit risk. It is responsible for overseeing the process of credit analysis and internal rating (either using internal rating based on a statistical modeling systems, or to an expert).</p> <p>The estimation of specific impairments on the French local communities requires the identification of the assets exposed to credit risk, and a judgmental exercise of the Risks division to assess the incurred losses. We have regarded the estimate of specific impairments of the loans and advances to French local communities to be a significant risk to our accounting.</p>	<p>With the support of our experts in local public sector, our credit risk modelling expert and our IT specialists we have reviewed:</p> <ul style="list-style-type: none"> • the acquisition process of loans originally granted by LBP in order to assess the quality of the acquired loans; • the credit risk monitoring process, including by: <ul style="list-style-type: none"> - acknowledging the role of the specialized committees and the controls assessing the credit risk; - reviewing the minutes of these committees and the internal audit reports; - reviewing the follow-up process of high-risk structured loans as part of the desensitization policy; - analyzing the internal rating update process (frequency, criteria...); - reviewing the identification process of loans with a higher-risk profile that require an estimate of a specific depreciation; - reviewing healthy loans, via the selection of a panel, in order to ensure the correct classification of loans between healthy and doubtful loans; • the assessment process of the Risks division toward the determination of specific impairments on French local communities, which is based on their financial structure, in particular by: <ul style="list-style-type: none"> - testing, via a panel, for the determination of specific impairments ; - reviewing the contagion process of doubtful loans.

Verification of the Management Report and of the other documents provided to shareholders

We have also performed, in accordance with professional standards applicable in France, the specific verifications required by French law.

Information provided in the Management Report and in the other documents provided to the shareholders with respect to the financial position and the financial statements

We have no matters to report as to the fair presentation and the consistency with the financial statements of the information given in the management report of the Executive Board and in the other documents provided to shareholders with respect to the financial position and the financial statements.

Report on Corporate Governance

We attest that the Supervisory Board's Report on Corporate Governance sets out the information required by articles L.225-37-3 and L.225-37-4 of the Code of Commerce.

Concerning the information given in accordance with the requirements of article L.225-37-3 of the French Commercial Code (Code of Commerce) relating to remunerations and benefits received by the directors and any other commitments made in their favour, we have verified its consistency with the financial statements, or with the underlying information used to prepare these financial statements and, where applicable, with the information obtained by your company from controlling and controlled companies.

Based on this work, the accuracy and sincerity of these information lead us to make the following remark: as stated in the report of Corporate Governance, the information does not include salaries and benefits paid by the company controlling your company to corporate officers concerned in the title of their functions of employees or corporate officer of SFIL.

Report on other legal and regulatory requirements

Appointment of the statutory auditors

We were appointed as statutory auditors of Caisse Française de Financement Local (formerly Dexia Municipal Agency) by the annual general meeting held on May 26, 2008 for DELOITTE & ASSOCIÉS and on May 31, 2017 for ERNST & YOUNG et Autres.

As of December 31, 2017 DELOITTE & ASSOCIÉS was in the 10th year of total uninterrupted engagement and ERNST & YOUNG et Autres in the 1st year.

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with French accounting principles, 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.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless it is expected to liquidate the Company or to cease operations.

The Financial Statements Committee of SFIL entity, acting as the Financial Statements Committee of the Caisse Française de Financement Local, is responsible for monitoring the financial reporting process and the effectiveness of internal control and risks management systems and where applicable, its internal audit, regarding the accounting and financial reporting procedures.

The financial statements were approved by the Executive Board.

Statutory auditors' responsibilities for the audit of the financial statements

Objectives and audit approach

Our role is to issue a report on the financial statements. Our objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with professional standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As specified in article L.823-10-1 of the French Commercial Code (Code of Commerce), our statutory audit does not include assurance on the viability of the Company or the quality of management of the affairs of the Company.

As part of an audit conducted in accordance with professional standards applicable in France, the statutory auditor exercises professional judgment throughout the audit and furthermore:

- identifies and assesses the risks of material misstatement of the financial statements, whether due to fraud or error, designs and performs audit procedures responsive to those risks, and obtains audit evidence considered to be sufficient and appropriate to provide a basis for his opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- obtains an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control.
- evaluates the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management in the financial statements.
- assesses the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. This assessment is based on the audit evidence obtained up to the date of his audit report. However, future events or conditions may cause the Company to cease to continue as a going concern. If the statutory auditor concludes that a material uncertainty exists, there is a requirement to draw attention in the audit report to the related disclosures in the financial statements or, if such disclosures are not provided or inadequate, to modify the opinion expressed therein.
- evaluates the overall presentation of the financial statements and assesses whether these statements represent the underlying transactions and events in a manner that achieves fair presentation.

Report to the Financial Statements Committee of SFIL entity, acting as Financial Statements Committee of the Caisse Française de Financement Local

We submit a report to the Financial Statements Committee of SFIL entity, acting as Financial Statements Committee of the Caisse Française de Financement Local, which includes in particular a description of the scope of the audit and the audit program implemented, as well as the results of our audit. We also report, if any, significant deficiencies in internal control regarding the accounting and financial reporting procedures that we have identified.

Our report to the Financial Statements Committee of SFIL entity, acting as Financial Statements Committee of the Caisse Française de Financement Local, includes the risks of material misstatement that, in our professional judgment, were of most significance in the audit of the financial statements of the current period and which are therefore the key audit matters that we are required to describe in this report.

We also provide the Financial Statements Committee of SFIL entity, acting as Financial Statements Committee of the Caisse Française de Financement Local, with the declaration provided for in Article 6 of Regulation (EU) N°537/2014, confirming our independence within the meaning of the rules applicable in France such as they are set in particular by articles L.822-10 to L.822-14 of the French Commercial Code (Code of Commerce) and in the Code of Ethics (code de déontologie) for statutory auditors. Where appropriate, we discuss with the Financial Statements Committee the risks that may reasonably be thought to bear on our independence, and the related safeguards.

Neuilly-sur-Seine and Paris-La Défense, le 29 mars 2018

The statutory auditors

French original signed by:

DELOITTE & ASSOCIÉS
Sylvie Bourguignon

ERNST & YOUNG et Autres
Vincent Roty

Supplemental disclosures

Over-collateralization ratio

Pursuant to articles L.513-12 and R.513-8 of the Monetary and Financial Code, the total of the assets of *sociétés de crédit foncier* must always exceed by at least 5% liabilities benefiting from the privilege referred to in article L.513-11 of the Monetary and Financial Code.

Assets covering liabilities benefiting from the privilege (weighted amounts in EUR millions)	12/31/2017
Exposures on public sector entities	53,535
Shares in funds or similar entities that meet the conditions of L.513-5 of the Monetary and Financial Code	-
Replacement assets	925
Other assets	2,976
Operations deducted from the assets	-
TOTAL ASSETS	57,436
Liabilities benefiting from the privilege defined in article L.513-11 of the Monetary and Financial Code (weighted amounts in EUR millions)	12/31/2017
<i>Obligations foncières</i>	42,794
Other bonds benefiting from the privilege	6,415
Liabilities related to these securities	741
Amounts owed under the contract provided for in article L.513-15 of the Monetary and Financial Code	23
Amounts owed for derivatives benefiting from the privilege defined in article L.513-11 of the Monetary and Financial Code	1,483
Debt attributable to miscellaneous expense mentioned in the last section of the article L.513-11 of the Monetary and Financial Code	0
TOTAL LIABILITIES	51,456
OVER-COLLATERALIZATION RATIO	111.6%

Statutory auditors' fees in 2017

EUR thousands	Mazars				Deloitte & Associés				Ernst & Young et Autres			
	Amount including VAT		%		Amount including VAT		%		Amount including VAT		%	
	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017
Audit services rendered												
Audit, certification, examination of company financial statements	258	-	79%	-	258	240	79%	83%	-	240	-	91%
Other audit tasks	70	-	21%	-	70	50	21%	17%	-	23	-	9%
Sub-total	328	-	100%	-	328	290	100%	100%	-	263	-	100%
Other services												
Legal, tax, labor issues	-	-	-	-	-	-	-	-	-	-	-	-
Internal audit	-	-	-	-	-	-	-	-	-	-	-	-
Other (to specify if > 10% of audit fees)	-	-	-	-	-	-	-	-	-	-	-	-
Sub-total	-	-	-	-	-	-	-	-	-	-	-	-
TOTAL	328	-	100%	-	328	290	100%	100%	-	263	-	100%

Additional responsibilities principally cover expenses related to the review of issue programs and comfort letters to public issues.

Shareholders Meeting of May 28, 2018

Statutory Auditors' special report on regulated agreements and commitments Shareholders' Meeting held to approve the financial statements for the year ended December 31, 2017

This is a free translation into English of the statutory auditors' special report on regulated agreements and commitments issued in French and it is provided solely for the convenience of English speaking users. This report should be read in conjunction and construed in accordance with French law and the relevant professional standards applicable in France.

To the Shareholder's Meeting of Caisse Française de Financement Local,

In our capacity as Statutory Auditors of your Company, we hereby report to you on regulated agreements and commitments.

The terms of our engagement require us to communicate to you, based on information provided to us, the principal terms and conditions of those agreements and commitments brought to our attention or which we may have discovered during the course of our audit, without expressing an opinion on their usefulness and appropriateness or identifying such other agreements and commitments, if any. It is your responsibility, pursuant to article R.225-58 of the French Commercial Code (*Code de Commerce*), to assess the interest involved in respect of the conclusion of these agreements and commitments for the purpose of approving them.

Our role is also to provide you with the information stipulated in article R.225-58 of the French Commercial Code relating to the implementation during the past year of agreements and commitments previously approved by the Shareholders' Meeting, if any.

We conducted the procedures we deemed necessary in accordance with the professional guidelines of the French National Institute of Statutory Auditors (*Compagnie Nationale des Commissaires aux Comptes*) relating to this engagement.

AGREEMENTS AND COMMITMENTS SUBMITTED TO THE APPROVAL OF THE SHAREHOLDERS' MEETING

We hereby inform you that we have not been advised of any agreement or commitment authorized and signed during the year to be submitted to the approval of the Shareholders' Meeting pursuant to article L.225-86 of the French Commercial Code.

AGREEMENTS AND COMMITMENTS PREVIOUSLY APPROVED BY THE SHAREHOLDERS' MEETING

We hereby inform you that we have not been advised of any agreement or commitment previously approved by the Shareholders' Meeting which remained in force during the year.

Paris-la-Défense and Neuilly-sur-Seine, on March 29, 2018

The statutory auditors

French original signed by:

ERNST & YOUNG et Autres
Vincent Roty

DELOITTE & ASSOCIÉS
Sylvie Bourguignon

Observations of the Supervisory Board

Pursuant to the provisions of article L.225-68 of the Code of Commerce, we hereby state that we have no comment to make on the management report of the Executive Board or on the financial statements for the year ended December 31, 2017.

The Supervisory Board wishes to thank the Executive Board for the initiatives taken and the results achieved during the year ended December 31, 2017.

The Supervisory Board

Resolutions proposed to the Ordinary and Extraordinary Shareholders' Meeting of May 28, 2018

To the Ordinary Shareholders' Meeting

First resolution: approval of the financial statements

The Shareholders' Meeting, voting according to the conditions governing the quorum and majority required for ordinary shareholders' meetings, after hearing the reports of the Executive Board, the Chairman of the Supervisory Board and the statutory auditors, as well as the observations of the Supervisory Board, approves the financial statements for the year ended December 31, 2017, as presented, with all the transactions that generated these financial statements or are mentioned in the above reports, showing a net income of EUR 29,705,091.31.

The Shareholders' Meeting notes that no expense mentioned in article 39, 4 of the French General Tax Code, non-deductible from corporate income tax, was recorded in the year ended December 31, 2017.

Second resolution: allocation of net income

The Shareholders' Meeting, voting according to the conditions governing the quorum and majority required for ordinary shareholders' meetings, resolves to allocate the net income for the year as follows.

ALLOCATION OF NET INCOME	EUROS
Net income for the year	29,705,091.31
Legal reserve (5%)	(1,485,254.57)
Income available	28,219,836.74
Retained earnings	23,640,014.37
Income available for distribution	51,859,851.11
Dividends distributed	(49,950,000.00)
Retained earnings after allocation	1,909,851.11

Each share will receive a dividend of EUR 3.70 eligible for a rebate of 40% according to article 158.3-2° of the French General Tax Code (Code Général des Impôts).

The dividend will be paid on June 6, 2018.

The Ordinary Shareholders' Meeting recalls, in accordance with article 243 bis of the French General Tax Code (Code Général des Impôts) that the following dividends were paid corresponding to the previous three years:

EUR	2015	2016	2017
Net amount per share	-	-	2.67
Amount per share eligible for a rebate (article 158.3-2° of the French General Tax Code)	-	-	2.67 ⁽¹⁾
Total amount eligible for a rebate (article 158.3-2° of the French General Tax Code)	-	-	35,110,500 ⁽¹⁾

⁽¹⁾ rate of 40%.

Third resolution: approval of regulated agreements and commitments

After hearing the statutory auditors' special report on regulated agreements and commitments, governed by article L.225-86 of the Code of Commerce, the Shareholders' Meeting, voting according to the conditions governing the quorum and majority required for ordinary shareholders' meetings, notes, under the conditions of article L.225-88 of the same code, that no agreement was mentioned with reference to the year ended December 31, 2017.

Fourth resolution: discharge to members of the management bodies

The Shareholders' Meeting, voting according to the conditions governing the quorum and majority required for ordinary shareholders' meetings, gives full discharge to the management bodies for the performance of their duties during the year ended December 31, 2017.

Fifth resolution: certification of the financial statements

In application of article L.822-14 of the Code of Commerce, the Shareholders' Meeting, voting according to the conditions governing the quorum and majority required for ordinary shareholders' meetings, takes note that the financial statements for the year ended December 31, 2017, were certified by the statutory auditors:

- Sylvie Bourguignon, Partner, representing the firm Deloitte & Associés, on one hand,
- Vincent Roty, Partner, representing the firm Ernst & Young et Autres, on the other hand.

To the Extraordinary Shareholders' Meeting

Sixth resolution: change in article 4 of the by-laws "Headquarters"

The Shareholders' Meeting, voting according to the conditions governing the quorum and majority required for extraordinary shareholders' meetings, after hearing the report of the Executive Board,

decides to change article 4 of the by-laws ("Headquarters") in order to foresee the possibility offered to the Supervisory Board by article L.225-65 of the Code of Commerce to transfer headquarters over the whole territory of France, and

decides consequently to replace article 4 of the Company's by-laws by the following article.

"Article 4 - HEADQUARTERS

The Company's headquarters is set at 1-3, rue du Passeur de Boulogne - 92130 Issy-les-Moulineaux.

It may be transferred within the territory of France by a decision of the Supervisory Board, subject to the ratification of this decision by the next ordinary shareholders' meeting. In the event of a transfer decided in accordance with current legislation by the Supervisory Board, the latter is authorized to change the by-laws in consequence."

Seventh resolution: powers

The Shareholders' Meeting, voting according to the conditions governing the quorum and majority required for extraordinary shareholders' meetings, gives full powers to the bearer of an original, a copy or an excerpt of the minutes of this meeting to carry out all legal formalities in respect of registration and publication required by laws.

General Information

Legal and administrative information

Corporate name

Caisse Française de Financement Local

Acronym

CAFFIL

Registered office

Since December 1, 2014, the Company's registered office is located at
1-3, rue du Passeur de Boulogne
92130 Issy-les-Moulineaux

Legal structure

Société anonyme à directoire et conseil de surveillance, a joint-stock corporation with an Executive Board and a Supervisory Board.

Official approval

The Company was approved by the Comité des établissements de crédit et des entreprises d'investissement (CECEI) on July 23, 1999, as a *société financière – société de crédit foncier*. This approval became definitive on October 1, 1999. *Ordonnance* 2013-544 of June 27, 2013, modified the legal status of *sociétés de crédit foncier* (article L.513-2 of the Monetary and Financial Code). Since January 1, 2014, *sociétés de crédit foncier* are no longer financial companies (*sociétés financières*), but specialized credit institutions (*établissements de crédit spécialisés*).

Applicable legislation

A corporation under the provisions of articles L.210-1 and following of the Code of Commerce, articles L.511-1 and following of the Monetary and Financial Code and articles L.513-2 and following of the Monetary and Financial Code.

Incorporation date

The Company was created on December 29, 1998, for a period of 99 years.

Corporate purpose (article 2 of the by-laws)

The Company's exclusive purpose is:

- to grant or acquire exposures on public sector entities as defined in article L.513-4 of the Monetary and Financial Code as well as shares and units of assets considered as exposures on public sector entities as defined in article L.513-5 of the same code;
- to hold assets, securities and deposits according to the conditions defined by decree to be considered as replacement assets;
- in order to finance the above-mentioned exposures, to issue *obligations foncières* benefiting from the privilege defined in article L.513-11 of the Monetary and Financial Code and finance and raise other funds, for which the contract or document intended for the general public in the sense of article L.412-1 of the Monetary and Financial Code, or any equivalent document required for admission to foreign regulated markets mentions this privilege.

The Company may also fund the above-mentioned activities by issuing bonds or other sources of financing that do not benefit from the privilege defined in article L.513-11 of the Monetary and Financial Code.

The Company may mobilize, in accordance with articles L.211-36 to L.211-40 of the Monetary and Financial Code or in accordance with articles L.313-23 to L.313-35 of the Monetary and Financial Code, all or part of the assets it holds, whatever the nature, be it professional or not, of these assets.

Within the framework of the achievement of the exclusive purpose mentioned above, the Company may conduct all related operations linked directly or indirectly to its activities or contributing to this exclusive objective, as long as these operations are carried out in accordance with the terms of articles L.513-2 and following and R.513-1 and following of the Monetary and Financial Code related to *sociétés de crédit foncier*.

Company registration and APE business identification code

Caisse Française de Financement Local is registered as a corporate entity under the designation NANTERRE 421 318 064 (Registre du Commerce et des Sociétés). Its APE code is 6492Z.

Availability of information

Legal documents concerning Caisse Française de Financement Local may be consulted at the Company's registered office:
1-3, rue du Passeur de Boulogne
92130 Issy-les-Moulineaux

Fiscal year (article 38 of the by-laws)

The Company's fiscal year begins on January 1 and ends on December 31.

Exceptional events and legal proceedings

See the section on litigation in part 9.2.5. of the management report of this annual financial report.

Allocation of income (article 39 of the by-laws)

Income available for distribution comprises net income for the year minus any prior year losses and any allocations to reserves pursuant to current legislation, plus any retained earnings carried forward from previous years.

From the available surplus, the Ordinary Shareholders' Meeting, voting on a recommendation of the Executive Board, may allocate all or a part of the remaining income to retained earnings.

There are no priority shares or priority dividends.

Annual Shareholders' Meetings**Calling of meetings (article 27 of the by-laws)**

Annual shareholders' meetings are called as required by current legislation. They are held at the Company's registered office or any other location specified in the notice of meeting.

All shareholders have the right to obtain copies of the documents required to make an informed decision concerning the overall management and control of the Company.

The types of documents concerned and the terms of their availability and dispatch are determined by applicable legislation and regulations.

Right to attend annual shareholders' meetings

Legal rights apply.

Voting rights (article 31 of the by-laws)

The voting rights attached to the shares are proportional to the percentage of capital the shares represent. Each share conveys one voting right. At annual shareholders' meetings, the number of votes that may be cast by each shareholder corresponds to the number of shares held plus the number of shares for which the shareholder holds proxy.

Capital and shares**Amount of the capital**

Share capital currently stands at EUR 1,350,000,000 represented by 13,500,000 nominative shares with a face value of EUR 100.

There are no other securities that grant rights to shares in the capital of Caisse Française de Financement Local.

Capital in the last five years

Date of the Extraordinary Shareholders' Meeting	Date of the capital increase	Amount of the capital increase EUR	Cumulated capital EUR
5/24/13	-	-	1,315,000,000
5/22/14	-	-	1,315,000,000
5/26/15	-	-	1,315,000,000
5/25/16	-	-	1,315,000,000
5/30/17	6/08/17	35,000,000	1,350,000,000

Breakdown of capital	2013	2014	2015	2016	2017
SFIL	99.99%	99.99%	99.99%	99.99%	99.99%
Individual investors	0.01%	0.01%	0.01%	0.01%	0.01%

From January 31, 2013 to May 18, 2016, Caisse Française de Financement Local was 99.99%-owned by SFIL (previously denominated Société de Financement Local), and 0.01% of its capital was in the hands of private investors (individuals, members of the Supervisory Board, to whom SFIL had lent shares).

Since May 18, 2016, only one individual, a member of the Supervisory Board, has kept a share of the Company (lent by SFIL as a *prêt de consommation d'action*).

Declaration of financial support

On January 31, 2013, SFIL (previously denominated Société de Financement Local) formalized a declaration of financial support for its subsidiary Caisse Française de Financement Local.

“Société de Financement Local acquired Caisse Française de Financement Local, previously called Dexia Municipal Agency, a société de crédit foncier, governed by articles L.515-13⁽¹⁾ and following of the Monetary and Financial Code.

“Société de Financement Local will hold more than 99% of the capital of Caisse Française de Financement Local on a long-term basis.

“Société de Financement Local and the French State, its reference shareholder, will ensure that Caisse Française de Financement Local always be able to pursue its activity in an ongoing manner and honor its financial commitments, in compliance with the requirements of banking regulations currently in effect.”

Management
ReportCorporate
Governance ReportFinancial Statements
in accordance
with IFRSFinancial Statements
in accordance
with french GAAPSupplemental
DisclosuresShareholders'
Meeting

General Information

(1) Now article L.513-2 of the Monetary and Financial Code in application of ordonnance 2013-544 of June 27, 2013.

Statement by the person responsible

I, Gilles Gallerne, Chairman of the Executive Board of Caisse Française de Financement Local, hereby affirm that to the best of my knowledge, the financial statements have been prepared in conformity with applicable accounting standards and present fairly, in all material aspects, the assets and liabilities, financial position and results of Caisse Française de Financement Local, and that the management report presents a fair image of trends in the Company's business, results and financial position, as well as a description of the main risks and uncertainties it faces.

Issy-les-Moulineaux, March 29, 2018

Gilles Gallerne
Chairman of the Executive Board

Caisse Française de Financement Local

Société anonyme à directoire et conseil de surveillance

A French credit institution with an Executive Board and a Supervisory Board

Capital of EUR 1,350,000,000

R.C.S. NANTERRE 421 318 064

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This annual financial report is available in French and in English at

www.caissefrancaisedefinancementlocal.fr

www.caffil.fr

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